HARLEYSVILLE
FINANCIAL CORPORATION

2019
Annual Report

HARLEYSVILLE FINANCIAL CORPORATION
2019 ANNUAL REPORT

TABLE OF CONTENTS

CORPORATE PROFILE

Harleysville Financial Corporation, formerly Harleysville Savings Financial Corporation, (the "Company") is a Pennsylvania corporation headquartered in Harleysville, Pennsylvania. The Company became the bank holding company for Harleysville Bank, formerly Harleysville Savings Bank, in connection with the holding company reorganization of the Bank in February 2000 (the "Reorganization"). In August 1987, the Bank's predecessor, Harleysville Savings Association, converted to the stock form of organization. The Bank, whose predecessor was originally, incorporated in 1915, converted from a Pennsylvania chartered, permanent reserve fund savings association to a Pennsylvania chartered stock savings bank in June 1991. The Bank operates from six full-service offices located in Montgomery County and one office located in Bucks County, Pennsylvania. The Bank's primary market area includes Montgomery County, which has the third largest population and the second highest per capita income in the Commonwealth of Pennsylvania, and, to a lesser extent, Bucks County. As of September 30, 2019, the Company had $779.3 million of total assets, $586.3 million of deposits and $76.2 million of stockholders' equity. The Company's stockholders' equity constituted 9.8% of total assets as of September 30, 2019.

The Bank's primary business consists of attracting deposits from the general public and business customers through a variety of deposit programs and investing such deposits principally in first mortgage loans secured by residential properties in the Bank's primary market area. The Bank also originates a variety of consumer loans, predominately home equity loans and lines of credit also secured by residential properties in the Bank's primary lending area. The Bank is also engaged in the general commercial banking business, and provides a full range of commercial loans and commercial real estate loans to customers in the Bank's primary market area. The Bank serves its customers through its full-service branch network, the internet, telephone and mobile banking.

Deposits with the Bank are insured to the maximum extent provided by law through the Deposit Insurance Fund administered by the Federal Deposit Insurance Corporation ("FDIC"). The Bank is subject to examination and comprehensive regulation by the FDIC and the Pennsylvania Department of Banking ("Department"). It is also a member of the Federal Home Loan Bank of Pittsburgh ("FHLB of Pittsburgh" or "FHLB"), which is one of the 11 regional banks comprising the Federal Home Loan Bank System ("FHLB System"). The Bank is also subject to regulations of the Board of Governors of the Federal Reserve System ("Federal Reserve Board") governing reserves required to be maintained against deposits and certain other matters.

The Company's principal executive offices are located at 271 Main Street, Harleysville, Pennsylvania 19438 and its telephone number is (215) 256-8828.

Competition

The Company faces significant competition in attracting deposits. Its most direct competition for deposits has historically come from commercial banks and savings institutions located in its market area. The Company faces additional significant competition for investors' funds from other financial intermediaries. The Company competes for deposits principally by offering depositors a variety of deposit programs, convenient branch locations, hours and other services. The Company does not rely upon any individual group or entity for a material portion of its deposits.

The Company's competition for real estate loans comes principally from mortgage banking companies, other savings institutions, commercial banks and credit unions. The Bank competes for loan originations primarily through the interest rates and loan fees it charges, the efficiency and quality of services it provides borrowers, referrals from real estate brokers and builders, and the variety of its products. Factors which affect competition include the general and local economic conditions, current interest rate levels and volatility in the mortgage markets.

STOCK MARKET INFORMATION

Harleysville Financial Corporation's common stock trades on the OTC Bulletin Board under the symbol "HARL". Prices shown below reflect the prices reported on the OTC Bulletin Board during the indicated periods. The closing price of the common stock on September 30, 2019 was $22.80 per share. There were 3,764,057 shares of common stock outstanding as of September 30, 2019, held by approximately 1,000 stockholders of record, not including the number of persons or entities whose stock is held in nominee or "street" name through various brokerage firms and banks.

For The Quarter Ended	High	Low	Close	Cash Dividends Declared
September 30, 2019	**$24.40**	**$22.77**	**$22.80**	**$0.25**
June 30, 2019	**25.00**	**23.25**	**23.30**	**0.25**
March 31, 2019	**27.00**	**23.00**	**23.55**	**0.25**
December 31, 2018	**24.45**	**23.00**	**23.30**	**0.23**
September 30, 2018	$25.20	$22.81	$25.00	$0.23
June 30, 2018	24.25	23.50	24.00	0.23
March 31, 2018	23.55	22.34	23.55	0.23
December 31, 2017	23.00	21.85	23.00	0.22

Management's Discussion and Analysis of Financial Condition and Results of Operations.

The following discussion is intended to assist in understanding the financial condition, and the results of operations for Harleysville Financial Corporation, and its subsidiary Harleysville Bank, for the fiscal years ended September 30, 2019 and 2018. The information in this section should be read in conjunction with the Company's financial statements and the accompanying notes included elsewhere herein.

Overview

Harleysville Financial Corporation, a bank holding company, of which Harleysville Bank (the "Bank"), is a wholly owned subsidiary, was formed in February 2000. For purposes of this discussion, the Company, including its wholly owned subsidiary, will be referred to as the "Company." The Company's earnings are primarily dependent upon its net interest income, which is determined by (i) the difference between yields earned on interest-earning assets and rates paid on interest-bearing liabilities ("interest rate spread") and (ii) the relative amounts of interest-earning assets and interest-bearing liabilities outstanding. The Company's interest rate spread is affected by regulatory, economic, and competitive factors that influence interest rates, loan demand and deposit flows. The Company, like other institutions, is vulnerable to an increase in interest rates to the extent that interest-bearing liabilities mature or reprice more rapidly than interest-earning assets. To reduce the effect of adverse changes in interest rates on its operations, the Company has adopted certain asset and liability management strategies, described below. The Company's earnings are also affected by, among other factors, other non-interest income, other expenses, and income taxes.

The Company's total assets at September 30, 2019 amounted to $779.3 million compared to $768.9 million as of September 30, 2018. The increase in assets was primarily due to an increase in cash and investments of $23.0 million. The increase was partially offset by a decrease in loans receivable of $11.1 million. Total liabilities at September 30, 2019 were $703.0 million compared to $697.0 million at September 30, 2018. The increase in liabilities was due to an increase in total deposits of $4.3 million and an increase in borrowings of $2.6 million. Stockholders' equity totaled $76.2 million at September 30, 2019 compared to $71.8 million at September 30, 2018.

During fiscal 2019, net interest income increased $1.0 million or 4.3% from the prior fiscal year. This increase was primarily due to an increase in the interest rate spread to 3.03% in fiscal year 2019 from 2.95% in fiscal year 2018. There was a 1.4% increase in the average interest-earning assets and a 1.3% increase in average interest-bearing liabilities. Net income for fiscal 2019 was $8.1 million compared to $7.1 million for the fiscal year ended 2018. The Company's return on average assets (net income divided by average total assets) was 1.0% during fiscal 2019 compared to 0.9% during fiscal 2018. Return on average equity (net income divided by average equity) was 11.0% during fiscal 2019 compared to 10.2% during fiscal 2018.

Results of Operations

The following table sets forth as of the periods indicated, information regarding: (i) the total dollar amounts of interest income from interest-earning assets and the resulting average yields; (ii) the total dollar amount of interest expense on interest-bearing liabilities and the resulting average costs; (iii) net interest income; (iv) interest rate spread; (v) net interest-earning assets; (vi) the net yield earned on interest-earning assets; and (vii) the ratio of total interest-earning assets to total interest-bearing liabilities. Average balances are calculated on a monthly basis. Yields on tax-exempt assets have not been calculated on a fully tax-exempt basis.

	For The Year Ended September 30,					
	2019			2018		
	Average Balance	**Interest**	**Yield/Rate**	**Average Balance**	**Interest**	**Yield/Rate**
Interest-earning assets:						
Mortgage loans (2)(3)	**$326,141**	**$ 14,623**	**4.48%**	$319,370	$ 14,316	4.48%
Mortgage-backed securities	**89,397**	**2,050**	**2.29%**	100,431	2,219	2.21%
Commercial loans (3)	**208,358**	**9,603**	**4.61%**	194,142	8,712	4.49%
Consumer and other loans (3)	**97,778**	**4,065**	**4.16%**	103,480	3,994	3.86%
Investments	**42,781**	**1,283**	**3.00%**	36,273	1,088	3.00%
Total interest-earning assets	**764,455**	**31,624**	**4.13%**	753,696	30,329	4.02%
Interest-bearing liabilities:						
Savings and money market	**214,396**	**1,441**	**0.67%**	227,653	1,400	0.61%
Checking	**121,526**	**23**	**0.02%**	123,174	29	0.02%
Certificates of deposit	**193,072**	**3,155**	**1.63%**	167,998	2,210	1.32%
Total deposits	**528,994**	**4,619**	**0.87%**	518,825	3,639	0.70%
Borrowings	**110,804**	**2,434**	**2.20%**	112,994	3,128	2.77%
Total interest-bearing liabilities	**639,798**	**7,053**	**1.10%**	631,819	6,767	1.07%
Net interest income/interest rate spread		**$ 24,571**	**3.03%**		$ 23,562	2.95%
Net interest-earning assets/net yield on interest-earning assets(1)	**$ 124,657**		**3.21%**	$ 121,877		3.13%
Ratio of average interest-earning assets to average interest-bearing liabilities			**119.5%**			119.3%

(1) Net interest income divided by average interest-earning assets.
(2) Loan fee income is immaterial to this analysis.
(3) There were 48 non-accruing loans totaling $9.2 million at September 30, 2019 and 46 non-accruing loans totaling $9.6 million at September 30, 2018.

Net Interest Income

Net interest income increased by $1.0 million or 4.3% in fiscal 2019, over the prior year. The increase in the net interest income in fiscal 2019 was due to an increase in the interest rate spread between interest earning assets and interest bearing liabilities due to the transformation of the balance sheet from wholesale to retail. The driving factors are further explained below under "- Interest Income" and "- Interest Expense."

Interest Income

Interest income on mortgage loans increased by $307,000 or 2.1% in fiscal 2019 from the prior year. During fiscal 2019, the average balance of mortgage loans increased $6.8 million or 2.1% while the yield remained unchanged. The majority of loans during the year were fixed rate mortgages. The decrease in interest on mortgage-backed securities reflects an increase in the yield of 8 basis points, with a decrease in the average balance of $11.0 million in fiscal 2019. During fiscal 2019, the consumer and other loan average balance decreased $5.7 million or 5.5% and the yield increased by 30 basis points. The increase in interest income on commercial loans during fiscal 2019 reflected an increase in average balance of $14.2 million, and an increase in yield of 12 basis points.

Interest and dividends on investments increased by $196,000 or 18.0% in fiscal 2019 from fiscal 2018. During fiscal 2019, the increase in income resulted from an increase in the average balance of $6.5 million or 17.9%.

Interest Expense

Interest expense on deposits increased $980,000 or 26.9% in fiscal 2019 as compared to the prior year. In fiscal 2019, the average balance of deposits increased by $10.2 million. The average rate paid on deposits increased to 0.9% for the year ended September 30, 2019 compared to 0.7% for year ended September 30, 2018. The increase in the average rate paid on deposits in fiscal 2019 was due to an increase in the average balance of certificates of deposits of $25.1million and an increase in interest expense on certificates of deposits of $945,000 attributable to promotional rate offerings.

Interest expense on borrowings decreased by $694,000 or 22.2% in fiscal 2019 compared to the prior year. The decrease in fiscal 2019 was primarily the result of a decrease in the average balance of borrowings of $2.2 million or 1.9%. This decrease in the average balance of borrowings was offset by an increase in deposits and a direct result of the transformation of the balance sheet from wholesale to retail.

Provision for Loan Losses

Management establishes reserves for losses on loans when it determines that losses are probable. The adequacy of loan loss reserves is based upon a regular monthly review of loan delinquencies and "classified assets", as well as local and national economic trends. The allowance for loan losses totaled $4.8 million at September 30, 2019, compared to $3.9 million for fiscal year ended September 30, 2018 or 0.8% and 0.6% of total loans at September 30, 2019 and 2018 respectively. The Company recorded a provision for loan losses of $982,000 in fiscal 2019 compared to $1.0 million in fiscal 2018. The provision for loan loss reflects the Company's analysis and review of its loan portfolio and assessment of the underlying risks associated with delinquent loans as well as loans classified for regulatory purposes. For additional analysis of the allowance refer to Note 4 – Loans Receivable in the Consolidated Financial Statements.

Other Income

The Company's total other income increased to $3.1 million in fiscal 2019 compared to $2.9 million in fiscal 2018. The increase in other income is primarily due to an increase in gain on sale of foreclosed real estate of $467,000 in fiscal 2019 compared to $304,000 in fiscal 2018. In fiscal 2019 there was an increase in gain on sales of mortgage-backed securities of $144,000 compared to none in fiscal 2018.

Customer service fees and debit card income were $1.4 million in fiscal 2019 and 2018.

Other, which consists primarily of loan servicing fees, the sale of non-deposit products, and insurance commissions, decreased by $196,000 or 23.9% during fiscal 2019. The fees, which comprise other income, are set by the Company at a level that is intended to cover the cost of providing the related services and expenses to customers.

Other Expenses

Salaries and employee benefits increased by $249,000 or 2.9% in fiscal 2019 as compared to fiscal 2018. The increased expenses of salaries and employee benefits during the periods are attributable to an increase in staffing and normal salary increases.

Occupancy and equipment expense decreased $34,000 or 2.5% in fiscal year 2019 as compared to fiscal 2018. Data processing costs increased by $4,000 in fiscal 2019.

Other expenses, which consist primarily of advertising expenses, directors' fees, ATM network fees, professional fees, checking account costs, rewards expenses, REO expenses and stockholders expense decreased by $117,000 or 3.1% in fiscal 2019 compared to fiscal 2018. The decrease in other expenses in 2019 was attributable to a decrease in commercial loan expense, REO expense, legal expense and loan collection expense.

Deposit insurance premiums for the fiscal year 2019 decreased $265,000 or 88.0% from fiscal 2018. The Bank benefitted from an FDIC assessment credit and management decided to reinvest those funds in community contributions. The FDIC insurance assessment regulations provided that after the reserve ratio reached 1.38%, the FDIC would apply small bank credits to reduce small banks regular deposit insurance assessments up to the full amount of the assessments or the full amount of the credit whichever is less. The reserve ratio reached 1.40% on June 30, 2019.

Income Taxes

The Company recorded income tax provisions of $3.1 million in fiscal year 2019 and $2.9 million in 2018. The effective tax rate was 27.3% in fiscal 2019 compared to 28.8% in fiscal 2018. See Note 8 of the Consolidated Financial Statements which provides an analysis of the provision for income taxes.

INDEPENDENT AUDITOR'S REPORT

Audit Committee
Harleysville Financial Corporation
Harleysville, Pennsylvania

Report on the Financial Statements

We have audited the accompanying consolidated financial statements of Harleysville Financial Corporation and subsidiaries, which comprise the consolidated statement of financial condition, as of September 30, 2019 and 2018; the related consolidated statements of income, comprehensive income, stockholders' equity, and cash flows for the years then ended; and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements, in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

S.R. Snodgrass, P.C. • 2009 Mackenzie Way, Suite 340 • Cranberry Township, Pennsylvania 16066 • Phone: 724-934-0344 • Fax: 724-934-0345

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Harleysville Financial Corporation and subsidiaries as of September 30, 2019 and 2018, and the results of their operations and their cash flows for the years then ended, in accordance with accounting principles generally accepted in the United States of America.

S.R. Snodgrass, P.C.

Cranberry Township, Pennsylvania
December 3, 2019

Consolidated Statements of Financial Condition

(In thousands, except share data)	September 30, 2019	2018
Assets		
Cash and amounts due from depository institutions	**$ 2,740**	$ 2,867
Interest-bearing demand deposits	**18,547**	5,209
Total cash and cash equivalents	**21,287**	8,076
Investments and mortgage-backed securities:		
Available for sale (amortized cost – 2019, $3,222; 2018, $859)	**3,235**	876
Held to maturity (fair value – 2019, $115,447; 2018, $103,946)	**114,415**	107,042
Loans receivable (net of allowance for loan losses - 2019, $4,757; 2018, $3,922)	**604,784**	615,899
Accrued interest receivable	**2,079**	2,239
Federal Home Loan Bank stock - at cost	**5,058**	5,286
Foreclosed real estate	**-**	1,043
Office properties and equipment, net	**10,285**	10,631
Bank-owned life insurance	**16,862**	16,464
Prepaid expenses and other assets	**1,251**	1,309
TOTAL ASSETS	**$ 779,256**	$ 768,865
Liabilities and Stockholders' Equity		
Liabilities:		
Deposits	**$ 586,342**	$ 582,078
Short-term borrowings	**8,830**	17,207
Long-term debt	**102,295**	91,309
Accrued interest payable	**223**	179
Advances from borrowers for taxes and insurance	**1,582**	1,473
Other liabilities	**3,737**	4,781
Total liabilities	**703,009**	697,027
Commitments and contingencies (Notes 13 & 14)	**-**	-
Stockholders' Equity:		
Preferred Stock: $.01 par value; 7,500,000 shares authorized; none issued	**-**	-
Common stock: $.01 par value; 15,000,000 shares authorized; 3,921,177 shares issued: shares outstanding 2019, 3,764,057; 2018, 3,744,046	**39**	39
Additional paid-in capital	**7,882**	8,208
Treasury stock, at cost (2019, 157,120 shares; 2018, 177,131 shares)	**(3,081)**	(3,359)
Retained earnings - partially restricted	**71,400**	66,939
Accumulated other comprehensive income	**7**	11
Total stockholders' equity	**76,247**	71,838
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	**$ 779,256**	$ 768,865

See notes to consolidated financial statements.

Consolidated Statements of Income

(In thousands, except share and per share data)	Year Ended September 30, 2019	2018
Interest and Dividend Income:		
Interest and fees on mortgage loans	**$ 14,623**	$ 14,316
Interest on commercial loans	**9,603**	8,712
Interest on consumer and other loans	**4,065**	3,994
Interest on mortgage-backed securities	**2,050**	2,219
Interest on taxable investments	**886**	655
Interest on tax-exempt investments	**388**	430
Dividends on investment securities	**9**	3
Total interest and dividend income	**31,624**	30,329
Interest Expense:		
Interest on deposits	**4,619**	3,639
Interest on short-term borrowings	**97**	106
Interest on long-term debt	**2,337**	3,022
Total interest expense	**7,053**	6,767
Net Interest Income	**24,571**	23,562
Provision for Loan Losses	**982**	1,040
Net Interest Income, after Provision for Loan Losses	**23,589**	22,522
Other Income:		
Customer service fees and debit card income	**1,449**	1,348
Realized gains on securities	**144**	-
Realized gains on sale of foreclosed real estate, net	**467**	304
Income on bank-owned life insurance	**398**	393
Other income	**625**	821
Total other income	**3,083**	2,866
Other Expenses:		
Salaries and employee benefits	**8,774**	8,525
Occupancy and equipment	**1,310**	1,344
Deposit insurance premiums	**35**	300
Data processing	**1,455**	1,451
Other	**3,885**	3,779
Total other expenses	**15,459**	15,399
Income before Income Tax Expense	**11,213**	9,989
Income tax expense	**3,064**	2,879
Net Income	**$ 8,149**	$ 7,110
Earnings Per Share:		
Basic	**$ 2.17**	$ 1.89
Diluted	**$ 2.13**	$ 1.85
Weighted Average Shares Outstanding:		
Basic	**3,757,413**	3,759,817
Diluted	**3,821,965**	3,844,533

See notes to consolidated financial statements.

Consolidated Statements of Comprehensive Income

(In thousands)	Year Ended September 30, 2019	2018
Net Income	**$ 8,149**	$ 7,110
Other Comprehensive Loss:		
Unrealized losses on available-for-sale-securities	**(4)**	(4)
Income tax effect	**-**	-
Other comprehensive loss, net of tax	**(4)**	(4)
Comprehensive income	**$ 8,145**	$ 7,106

See notes to consolidated financial statements.

Consolidated Statements of Stockholders' Equity

(In thousands, except share and per share data)

	Common Stock Shares Outstanding	Common Stock	Additional Paid-in Capital	Retained Earnings-Partially Restricted	Accumulated Other Comprehensive Income (Loss)	Treasury Stock	Total Stockholders' Equity
Balance at September 30, 2017	3,759,637	$ 39	$ 8,261	$ 63,257	$ 13	$ (2,670)	$ 68,900
Reclassification of certain income tax effects from accumulated other comprehensive income				(2)	2		-
Net income				7,110			7,110
Dividends - $.91 per share				(3,426)			(3,426)
Restricted stock awards	4,806		(86)			86	-
Stock based compensation			258				258
Treasury stock delivered under 401k	2,684		19			45	64
Treasury stock purchase	(60,816)					(1,461)	(1,461)
Treasury stock delivered under dividend reinvestment plan	8,449		42			155	197
Employee options exercised	29,286		(286)			486	200
Other comprehensive loss					(4)		(4)
Balance at September 30, 2018	3,744,046	39	8,208	66,939	11	(3,359)	71,838
Net income				**8,149**			**8,149**
Dividends - $.98 per share				**(3,688)**			**(3,688)**
Restricted stock awards	**5,670**		**(112)**			**112**	**-**
Stock based compensation			**309**				**309**
Treasury stock delivered under 401k	**4,063**		**15**			**81**	**97**
Treasury stock purchase	**(27,000)**					**(651)**	**(651)**
Treasury stock delivered under dividend reinvestment plan	**7,568**		**30**			**150**	**180**
Employee options exercised	**29,710**		**(568)**			**586**	**18**
Other comprehensive loss					**(4)**		**(4)**
Balance at September 30, 2019	**3,764,057**	**$ 39**	**$ 7,882**	**$ 71,400**	**$ 7**	**$ (3,081)**	**$ 76,247**

See notes to consolidated financial statements.

Consolidated Statements of Cash Flows

(In thousands)	Year Ended September 30, 2019	2018
Operating Activities:		
Net Income	**$ 8,149**	$ 7,110
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	**722**	739
Provision for loan losses	**982**	1,040
Deferred income taxes	**(92)**	(18)
Change in corporate tax rate	**-**	355
Gains on sales of securities	**(144)**	-
Gain on sale of foreclosed real estate	**(467)**	(304)
Amortization of deferred fees	**(154)**	(80)
Increase in cash surrender value of bank owned life insurance	**(398)**	(393)
Stock based compensation	**309**	258
Changes in assets and liabilities which provided (used) cash:		
Decrease in other liabilities	**(1,044)**	(1,577)
Decrease (increase) in prepaid expenses and other assets	**150**	(115)
Decrease (increase) in accrued interest receivable	**160**	(161)
Increase (decrease) in accrued interest payable	**44**	(277)
Net cash provided by operating activities	**8,217**	6,577
Investing Activities:		
Purchase of mortgage-backed securities held to maturity	**(32,740)**	-
Purchase of investment securities held to maturity	**(3,000)**	-
Purchase of investment securities available-for-sale	**(43,249)**	(18,650)
Purchase of FHLB stock	**(1,343)**	(2,882)
Redemption of FHLB stock	**1,571**	2,980
Principal collected on securities available for sale	**20**	-
Proceeds from the redemption of investment securities available-for-sale	**40,866**	18,666
Proceeds from maturities of investment securities held to maturity	**3,625**	935
Proceeds from sales of mortgage-backed securities held to maturity	**3,565**	-
Principal collected on mortgage-backed securities held to maturity	**21,321**	23,908
Proceeds from sale of foreclosed real estate	**1,792**	1,069
Decrease (increase) in loans, net	**10,005**	(33,395)
Purchase of premises and equipment	**(376)**	(428)
Net cash provided by (used in) investing activities	**2,057**	(7,797)
Financing Activities:		
Net decrease in demand deposits, NOW accounts and savings accounts	**(2,903)**	(9,657)
Net increase in certificates of deposit	**7,167**	42,980
Cash dividends	**(3,688)**	(3,426)
(Decrease) increase in short term borrowings	**(8,377)**	2,870
Proceeds from long-term debt	**12,000**	46,000
Repayment of long-term debt	**(1,014)**	(77,312)
Acquisition of treasury stock	**(651)**	(1,461)
Sale of treasury stock delivered under employee stock plans	**294**	461
Net increase in advances from borrowers for taxes and insurance	**109**	6
Net cash provided by financing activities	**2,937**	461
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	**13,211**	(759)
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	**8,076**	8,835
CASH AND CASH EQUIVALENTS AT END OF YEAR	**$ 21,287**	$ 8,076
Supplemental Disclosure of Cash Flow Information		
Cash paid during the period for:		
Interest	**$ 7,009**	$ 7,044
Income taxes	**2,772**	2,110
Non-cash transfer of loans to foreclosed real estate	**282**	979

See notes to consolidated financial statements

Notes to Consolidated Financial Statements

1. Nature of Operations and Organizational Structure

Harleysville Financial Corporation, formerly Harleysville Savings Financial Corporation, (the "Company") is a bank holding company that is regulated by the Federal Reserve Bank of Philadelphia. Harleysville Bank, formerly Harleysville Savings Bank, (the Bank) is a wholly owned subsidiary and is regulated by the FDIC and the Pennsylvania Department of Banking. The Bank is principally in the business of attracting deposits through its branch offices and investing those deposits, together with funds from borrowings and operations, primarily in single family residential, commercial, consumer loans and investments. The Bank's customers are primarily in southeastern Pennsylvania.

2. Summary of Significant Accounting Policies

Principles of Consolidation - The accompanying consolidated financial statements include the accounts of the Company, the Bank, and the Bank's wholly owned subsidiary, HSB Inc., a Delaware subsidiary which was formed in order to accommodate the transfer of certain assets, Freedom Financial Solutions LLC that allows the Company to offer non-deposit products and HARL, LLC that allows the Bank to invest in equity investments. All significant intercompany accounts and transactions have been eliminated in consolidation.

Use of Estimates in Preparation of the Consolidated Financial Statements - The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the Consolidated Statement of Financial Condition and the reported amounts of income and expenses during the reporting period. The most significant of these estimates and assumptions in the Company's consolidated financial statements is the allowance for loan losses and other-than-temporary impairment of investments. Actual results could differ from those estimates.

Significant Group Concentrations of Credit Risk - Most of the Company's activities are with customers located within the southeastern region of Pennsylvania. Note 3 discusses the types of securities that the Company invests in. Note 4 discusses the types of lending that the Company engages in. The Company does not have any significant concentrations to any one industry or customer.

Cash and Cash Equivalents - For purposes of the Consolidated Statements of Cash Flows, cash and cash equivalents include cash and amounts due from depository institutions, including interest-bearing demand deposits in banks with original maturities of less than 90 days.

Investment and Mortgage-Backed Securities - The Company classifies and accounts for debt and equity securities as follows:

Held to Maturity - Debt securities that management has the positive intent and ability to hold until maturity are classified as held to maturity and are carried at their remaining unpaid principal balance, net of unamortized premiums or unaccreted discounts. Premiums are amortized and discounts are accreted using the interest method over the estimated remaining term of the underlying security.

Available for Sale - Debt and equity securities that will be held for indefinite periods of time, including securities that may be sold in response to changes in market interest or prepayment rates, needs for liquidity and changes in the availability of and the yield of alternative investments are classified as available for sale. These assets are carried at fair value. Unrealized gains and losses are excluded from earnings and are reported net of tax in other comprehensive income. Realized gains and losses on the sale of investment securities are recorded as of the trade date, reported in the Consolidated Statements of Income and determined using the amortized cost of the specific security sold.

For all securities that are in an unrealized loss position for an extended period of time and for all securities whose fair value is significantly below amortized cost, the Company performs an evaluation of the specific events attributable to the market decline of the security. The Company considers the length of time and extent to which the security's fair value has been below cost as well as the general market conditions, industry characteristics, and the fundamental operating results of the issuer to determine if the decline is other-than-temporary. The Company also considers as part of the evaluation its intent and ability to hold the security and whether it is more likely than not that it will be required to sell the security before its fair value has recovered to a level at least equal to the amortized cost.

For debt securities, accounting guidance specifies that (a) if a company does not have the intent to sell a debt security prior to recovery and (b) it is more likely than not that it will not have to sell the debt security prior to recovery, the security would not be considered other-than-temporarily impaired unless there is a credit loss. When an entity does not intend to sell the security, and it is more likely than not, the entity will not have to sell the security before recovery of its cost basis, it will recognize the credit component of an other-than-temporary impairment of a debt security in earnings and the remaining portion in other comprehensive income. For held to maturity debt securities, the amount of an other-than-temporary impairment recorded in other comprehensive income for the noncredit portion of a previous other-than-temporary impairment should be amortized prospectively over the remaining life of the security on the basis of the timing of future estimated cash flows of the security.

When the Company determines that a security's unrealized loss is other-than-temporary, an impairment loss is recognized in the period in which the decline in value is determined to be other-than-temporary.

Loans - The Company grants commercial, mortgage and consumer loans to customers. A substantial portion of the loan portfolio is represented by mortgage loans throughout southeastern Pennsylvania. The ability of the Company's debtors to honor their contracts is dependent upon the general economic conditions in this area.

Loans that management has the intent and ability to hold for the foreseeable future or until maturity or pay-off are reported at their outstanding unpaid principal balances adjusted for charge-offs, the allowance for loan losses, and any deferred fees or costs on originated loans.

Interest Income on Loans - Interest income is accrued on the unpaid principal balance. Interest on loans is recognized as income when earned. The accrual of interest on loans is discontinued at the time the loan is 90 days delinquent unless the credit is well-secured and in process of collection. In all cases, loans are placed on nonaccrual or charged-off at an earlier date if collection of principal or interest is considered doubtful.

All interest accrued but not collected for loans that are placed on nonaccrual or charged off are reversed against interest income. The interest on these loans is accounted for on the cash-basis or cost-recovery method, until qualifying for return to accrual. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

Deferred Loan Fees - Loan origination fees, net of certain direct origination costs, are deferred and the balance is amortized to income as an adjustment over the life of the loan using the interest method.

Allowance for Loan Losses - The allowance for loan losses is established as losses are estimated to have occurred through a provision for loan losses charged to earnings. Loan losses are charged against the allowance when management believes the uncollectibility of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance. An allowance for loan losses is maintained at a level that management considers adequate to provide for losses based upon evaluation of known and inherent risks in the loan portfolio. The loan loss reserves are established as an allowance for estimated losses based on the probable losses of the loan portfolio. In assessing risk, management considers historical experience, volume and composition of lending conducted by the Company, industry standards, and status of nonperforming loans, general economic conditions as they relate to the Company's market area, and other factors related to the collectibility of the Company's loan portfolio.

The allowance for loan losses consists of three elements: (1) specific allowances for impaired loans; (2) a general valuation allowance on all classified loans which are not impaired; and (3) a general valuation allowance on the remainder of the loan portfolio. This is consistent with the regulatory method of classifying reserves. Although the amount of each element of the allowance is determined separately, the entire allowance for loan losses is available for the entire portfolio. An allowance for impaired loans is established in the amounts by which the discounted cash flows (or collateral value or observable market price) are lower than the carrying value of the loan. A general allowance is established for classified loans that are not impaired. These loans are segregated by loan category, and allowance percentages are assigned to each category based on inherent losses associated with each type of lending and consideration that these loans, in the aggregate, represent an above-average credit risk and that more of these loans will prove to be uncollectible compared to loans in the general portfolio.

Foreclosed Real Estate - Real estate acquired through, or in lieu of, loan foreclosures are carried at the lesser of cost or fair value of the property, based on an appraisal less cost to sell. Costs relating to the development and improvement of the property are capitalized, and those relating to holding the property are charged to expense. The Company had no foreclosed real estate as of September 30, 2019 compared to $1.0 million as of 2018, respectively.

Office Properties and Equipment - Land is carried at cost. Office properties and equipment are recorded at cost, less accumulated depreciation. Depreciation is computed using the straight-line method over the expected useful lives of the assets that range from four to forty years. The costs of maintenance and repairs are expensed as they are incurred, and renewals and betterments are capitalized.

Federal Home Loan Bank Stock - Federal law requires a member institution of the Federal Home Loan Bank (FHLB) to hold stock of its district FHLB according to a predetermined formula. The restricted stock is carried at cost.

Management's determination of whether these investments are impaired is based on their assessment of the ultimate recoverability of their cost rather than by recognizing temporary declines in value. The determination of whether a decline affects the ultimate recoverability of their cost is influenced by criteria such as (1) the significance of the decline in net assets of the FHLB as compared to the capital stock amount for the FHLB and the length of time this situation has persisted, (2) commitments by the FHLB to make payments required by law or regulation and the level of such payments in relation to the operating performance of the FHLB, and (3) the impact of legislative and regulatory changes on institutions and, accordingly, on the customer base of the FHLB.

Cash Surrender Value of Bank-Owned Life Insurance (BOLI) - The Bank funded the purchase of insurance policies on the lives of officers and employees of the Bank. The Company has recognized any increase in cash surrender value of life insurance, net of insurance costs, in the Consolidated Statements of Income as income on BOLI. The cash surrender value of the insurance policies is recorded as an asset in other assets in the Consolidated Statements of Financial Condition and amounted to $16.9 million and $16.5 million at September 30, 2019 and 2018, respectively.

Income Taxes - Deferred income taxes are recognized for the tax consequences of "temporary differences" by applying enacted statutory tax rates applicable to future years to differences between the financial statement carrying amounts and the tax bases of existing assets and liabilities. The effect on deferred taxes of a change in tax rates is recognized in income in the period that includes the enactment date. The Company and its subsidiary file a consolidated federal income tax return.

The Company analyzes each tax position taken in its tax returns and determines the likelihood that the position will be realized. Only tax positions that are "more likely than not" to be realized can be recognized in the Company's financial statements. For tax positions that do not meet this recognition threshold, the Company will record an unrecognized tax benefit for the difference between the position taken on the tax return and the amount recognized in the financial statements. The Company does not have any material unrecognized tax benefits or accrued interest or penalties at September 30, 2019 and 2018, or during the years then ended. No unrecognized tax benefits are expected to arise within the next twelve months. The Company's policy is to account for interest as a component of interest expense and penalties as a component of other expenses. The Company and its subsidiaries are subject to U.S. Federal income tax as well as income tax of the Commonwealth of Pennsylvania. The Company is no longer subject to examination by taxing authorities for the years before October 1, 2016.

On December 22, 2017, federal tax reform legislation, commonly referred to as the Tax Cuts and Jobs Act of 2017 (the "Tax Act"), was enacted. The Tax Act makes broad and complex changes to the U.S. tax code that affected our income tax rate in 2017. The Tax Act reduced the U.S. federal corporate income tax rate from 34% to 21%. As a result, the Company was required to re-measure, through income tax expense, the deferred tax assets and liabilities using the enacted rate at which they are expected to be recovered or settled. The re-measurement of the net deferred tax asset resulted in additional income tax expense of $355,000 for the year ended September 30, 2018.

Transfers of Financial Assets - Transfers of financial assets are accounted for as sales, when control over the assets has been surrendered. Control over transferred assets is deemed to be surrendered when (1) the assets have been isolated from the Company (2) the transferee obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets, and (3) the Company does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity.

Treasury Stock - The Company records treasury stock purchases at cost. Gains and losses on subsequent reissuance of shares are credited or charged to additional paid-in capital using the average-cost method.

Stock Based Compensation - The Company currently has several stock based compensation plans in place for employees and directors of the Company. The Company recognizes the cost of employee services received in exchange for an award of equity investment based on grant-date fair value of the award. That cost will be recognized over the period during which an employee is required to provide service in exchange for the award. Stock-based compensation expense for the years ended September 30, 2019 and 2018 was $309,000 and $258,000, respectively. The tax benefit recognized related to the compensation expense for the years ended September 30, 2019 and 2018 was $28,000 and $19,000, respectively.

Earnings Per Share - Basic earnings per common share is computed based on the weighted average number of shares outstanding. Diluted earnings per share is computed based on the weighted average number of shares outstanding, increased by additional common shares that would have been outstanding if dilutive potential common shares had been issued. Potential common shares that may be issued by the Company relate to outstanding stock options and unvested stock awards, and are determined using the treasury stock method. The number of anti-dilutive options that are excluded from the earnings per share calculation for the years ended September 30, 2019 and 2018 were 118,218 and 101,264, respectively. For the years ended September 30, 2019 and 2018, the exercise price for the options representing anti-dilutive shares ranged from $18.66 to $24.55. The weighted average shares outstanding used to calculate earnings per share were as follows:

	Year Ended September 30,	
	2019	**2018**
Weighted average shares outstanding – basic	**3,757,413**	3,759,817
Increase in shares due to dilutive potential common shares	**64,552**	84,716
Weighted average shares outstanding – diluted	**3,821,965**	3,844,533

Other Comprehensive Income (Loss) - The Company presents, as a component of comprehensive income, amounts from transactions and other events, which are currently excluded from the Consolidated Statements of Income and are recorded directly to stockholders' equity. The Company's other comprehensive income consists of net unrealized holding gains or losses on securities available-for-sale, net of income taxes.

Reclassifications - Certain amounts in the prior period's financial statements have been reclassified to conform with the current year classifications. The reclassifications had no effect on net income.

Adoption of New Accounting Standards - In May 2014, the FASB issued ASU No. 2014-09, *"Revenue from Contracts with Customers."* The standard's core principle is that a company will recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which the company expects to be entitled in exchange for those goods or services. In doing so, companies generally will be required to use more judgment and make more estimates than under current guidance. These may include identifying performance obligations in the contract, estimating the amount of variable consideration to include in the transaction price and allocating the transaction price to each separate performance obligation. Subsequent to the issuance of ASU 2014-09, the FASB issued targeted updates to clarify specific implementation issues including ASU No. 2016-08, "Principal versus Agent Considerations (Reporting Revenue Gross versus Net)," ASU No. 2016-10, *"Identifying Performance Obligations and Licensing,"* ASU No. 2016-12, *"Narrow-Scope Improvements and Practical Expedients,"* and ASU No. 2016-20 *"Technical Corrections and Improvements to Topic 606, Revenue from Contracts with Customers."* For financial reporting purposes, the standard allows for either full retrospective adoption, meaning the standard is applied to all of the periods presented, or modified retrospective adoption, meaning the standard is applied only to the most current period presented in the financial statements with the cumulative effect of initially applying the standard recognized at the date of initial application. Since the guidance does not apply to revenue associated with financial instruments, including loans and securities that are accounted for under other GAAP, the new guidance did not have a material impact on revenue most closely associated with financial instruments, including interest income and expense. The Company completed its overall assessment of revenue streams and review of related contracts potentially affected by the ASU, including deposit related fees, interchange fees, merchant income, and commissions. Based on this assessment, the Company concluded that ASU 2014-09 did not change the method in which the Company currently recognizes revenue for these revenue streams. The Company also completed its evaluation of certain costs related to these revenue streams to determine whether such costs should be presented as expenses or contra-revenue (i.e., gross vs. net). Based on its evaluation, the Company determined that the classification of these revenue streams will not change. The Company adopted ASU 2014-09 and its related amendments on its required effective date of October 1, 2018 utilizing the modified retrospective approach. Since there was no net income impact upon adoption of the new guidance, a cumulative effect adjustment to opening retained earnings was not deemed necessary. See Note 18 Revenue Recognition for more information.

In January 2016, the FASB issued ASU No. 2016-01, *"Recognition and Measurement of Financial Assets and Financial Liabilities."* This ASU addresses certain aspects of recognition, measurement, presentation, and disclosure of financial instruments by making targeted improvements to GAAP as follows: (1) require equity investments (except those accounted for under the equity method of accounting or those that result in consolidation of the investee) to be measured at fair value with changes in fair value recognized in net income. However, an entity may choose to measure equity investments that do not have readily determinable fair values at cost minus impairment, if any, plus or minus changes resulting from observable price changes in orderly transactions for the identical or a similar investment of the same issuer; (2) simplify the impairment assessment of equity investments without readily determinable fair values by requiring a qualitative assessment to identify impairment. When a qualitative assessment indicates that impairment exists, an entity is required to measure the investment at fair value; (3) eliminate the requirement to disclose the fair value of financial instruments measured at amortized cost for entities that are not public business entities; (4) eliminate the requirement for public business entities to disclose the method(s) and significant assumptions used to estimate the fair value that is required to be disclosed for financial instruments measured at amortized cost on the balance sheet; (5) require public business entities to use the exit price notion when measuring the fair value of financial instruments for disclosure purposes; (6) require an entity to present separately in other comprehensive income the portion of the total change in the fair value of a liability resulting from a change in the instrument-specific credit risk when the entity has elected to measure the liability at fair value in accordance with the fair value option for financial instruments; (7) require separate presentation of financial assets and financial liabilities by measurement category and form of financial asset (that is, securities or loans and receivables) on the balance sheet or the accompanying notes to the financial statements; and (8) clarify that an entity should evaluate the need for a valuation allowance on a deferred tax asset related to available-for-sale securities in combination with the entity's other deferred tax assets. The adoption of ASU No. 2016-01 on October 1, 2018 did not have a material impact on the Company's Consolidated Financial Statements. In accordance with (5) above, the Company measured the fair value of its loan portfolio as of September 30, 2019 using an exit price notion (see Note 16 Fair Value of Assets and Liabilities).

Recently Issued Accounting Standards - In February 2016, the FASB issued Accounting Standards Update (ASU) 2016-02, *Leases.* The new leases standard applies a right-of-use (ROU) model that requires a lessee to record, for all leases with a lease term of more than 12 months, an asset representing its right to use the underlying asset and a liability to make lease payments. For leases with a term of 12 months or less, a practical expedient is available whereby a lessee may elect, by class of underlying asset, not to recognize an ROU asset or lease liability. At inception, lessees must classify all leases as either finance or operating based on five criteria. Balance sheet recognition of finance and operating leases is similar, but the pattern of expense recognition in the income statement, as well as the effect on the statement of cash flows, differs depending on the lease classification. The new leases standard requires a lessor to classify leases as either sales-type, direct financing or operating, similar to existing U.S. GAAP. Classification depends on the same five criteria used by lessees plus certain additional factors. The subsequent accounting treatment for all three lease types is substantially equivalent to existing U.S. GAAP for sales-type leases, direct financing leases, and operating leases. However, the new standard updates certain aspects of the lessor accounting model to align it with the new lessee accounting model, as well as with the new revenue standard under Topic 606. Lessees and lessors are required to provide certain qualitative and quantitative disclosures to enable users of financial statements to assess the amount, timing, and uncertainty of cash flows arising from leases. The new leases standard addresses other considerations including identification of a lease, separating lease and non-lease components of a contract, sale and leaseback transactions, modifications, combining contracts, reassessment of the lease term, and re-measurement of lease payments. It also contains comprehensive implementation guidance with practical examples. The amendments are effective for public business entities for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. The amendments are effective for all other entities (including emerging growth entities as further described above) for fiscal years beginning after December 15, 2019, and interim periods within fiscal years beginning after December 15, 2020. Early adoption is permitted. Specific transition requirements apply. The Company's leases are operating leases and ASU 2016-02 will require us to add them to our Statement of Financial Condition. The Company's material operating leases are related to real estate. The impact to the Company's Statement of Financial Condition is approximately $3.1 million increase in assets and liabilities.

In June 2016, the FASB issued ASU 2016-13, *Financial Instruments – Credit Losses: Measurement of Credit Losses on Financial Instruments*, which changes the impairment model for most financial assets. This Update is intended to improve financial reporting by requiring timelier recording of credit losses on loans and other financial instruments held by financial institutions and other organizations. The underlying premise of the Update is that financial assets measured at amortized cost should be presented at the net amount expected to be collected, through an allowance for credit losses that is deducted from the amortized cost basis. The allowance for credit losses should reflect management's current estimate of credit losses that are expected to occur over the remaining life of a financial asset. The income statement will be effected for the measurement of credit losses for newly recognized financial assets, as well as the expected increases or decreases of expected credit losses that have taken place during the period. ASU 2016-13 is effective for annual and interim periods beginning after December 15, 2019, and early adoption is permitted for annual and interim periods beginning after December 15, 2018. With certain exceptions, transition to the new requirements will be through a cumulative effect adjustment to opening retained earnings as of the beginning of the first reporting period in which the guidance is adopted. On October 16, 2019, the FASB voted to defer the effective date for ASC 326, *Financial Instruments – Credit Losses*, for public business entities to fiscal years beginning after December 15, 2022, and interim periods within those fiscal years. The final ASU is expected to be issued in mid-November. We expect to recognize a one-time cumulative effect adjustment to the allowance for loan losses as of the beginning of the first reporting period in which the new standard is effective, but cannot yet determine the magnitude of any such one-time adjustment or the overall impact of the new guidance on the consolidated financial statements.

In March 2017, the FASB issued ASU 2017-08, *Receivables – Nonrefundable Fees and Other Costs (Subtopic 310-20).* The amendments in this Update shorten the amortization period for certain callable debt securities held at a premium. Specifically, the amendments require the premium to be amortized to the earliest call date. The amendments do not require an accounting change for securities held at a discount; the discount continues to be amortized to maturity. For public business entities, the amendments in this Update are effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018. For all other entities, the amendments are effective for fiscal years beginning after December 15, 2019, and interim periods within fiscal years beginning after December 15, 2020. Early adoption is permitted, including adoption in an interim period. If an entity early adopts the amendments in an interim period, any adjustments should be reflected as of the beginning of the fiscal year that includes that interim period. An entity should apply the amendments in this Update on a modified retrospective basis through a cumulative-effect adjustment directly to retained earnings as of the beginning of the period of adoption. Additionally, in the period of adoption, an entity should provide disclosures about a change in accounting principle. This Update is not expected to have a significant impact on the Company’s financial statements.

In August 2018, the FASB issued ASU 2018-13, *Fair Value Measurement (Topic 820): Disclosure Framework – Changes the Disclosure Requirements for Fair Value Measurements*. The Update removes the requirement to disclose the amount of and reasons for transfers between Level I and Level II of the fair value hierarchy; the policy for timing of transfers between levels; and the valuation processes for Level III fair value measurements. The Update requires disclosure of changes in unrealized gains and losses for the period included in other comprehensive income (loss) for recurring Level III fair value measurements held at the end of the reporting period and the range and weighted average of significant unobservable inputs used to develop Level III fair value measurements. This Update is effective for all entities for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2019. The Company is currently evaluating the impact the adoption of the standard will have on the Company’s financial statement disclosures.

In May 2019, the FASB issued ASU 2019-05, *Financial Instruments – Credit Losses, Topic 326*, which allows entities to irrevocably elect the fair value option for certain financial assets previously measured at amortized cost upon adoption of the new credit losses standard. To be eligible for the transition election, the existing financial asset must otherwise be both within the scope of the new credit losses standard and eligible for the applying the fair value option in ASC 825-10.3. The election must be applied on an instrument-by-instrument basis and is not available for either available-for-sale or held-to-maturity debt securities. For entities that elect the fair value option, the difference between the carrying amount and the fair value of the financial asset would be recognized through a cumulative-effect adjustment to opening retained earnings as of the date an entity adopted ASU 2016-13. Changes in fair value of that financial asset would subsequently be reported in current earnings. For entities that have not yet adopted ASU 2016-13, the effective dates and transition requirements are the same as those in ASU 2016-13. For entities that have adopted ASU 2016-13, ASU 2019-05 is effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. Early adoption is permitted once ASU 2016-13 has been adopted. On October 16, 2019, the FASB voted to defer the effective date for ASC 326, *Financial Instruments – Credit Losses*, for smaller reporting companies to fiscal years beginning after December 15, 2022, and interim periods within those fiscal years. The final ASU is expected to be issued in mid-November. This Update is not expected to have a significant impact on the Company's financial statements.

3. INVESTMENT AND MORTGAGE-BACKED SECURITIES

The amortized cost and fair value of the Company's securities with gross unrealized gains and losses, as of September 30, 2019 and 2018 are as follows:

Available for sale securities:

September 30, 2019 (In thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Collateralized mortgage obligations	**$ 765**	**$ 13**	**$ -**	**$ 778**
U.S. Government money market funds	**2,457**	**-**	**-**	**2,457**
Total Available for Sale Securities	**$ 3,222**	**$ 13**	**$ -**	**$ 3,235**

September 30, 2018 (In thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Collateralized mortgage obligations	$ 785	$ 17	$ -	$ 802
U.S. Government money market funds	74	-	-	74
Total Available for Sale Securities	$ 859	$ 17	$ -	$ 876

Held to maturity securities:

September 30, 2019 (In thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Mortgage-backed securities- U.S. Government Sponsored Enterprises (GSE'S)	**$ 94,745**	**$ 874**	**$ (183)**	**$ 95,436**
Collateralized mortgage obligations	**1,077**	**32**	**(1)**	**1,108**
Municipal bonds	**9,399**	**312**	**-**	**9,711**
U.S. Government Agencies	**9,194**	**2**	**(4)**	**9,192**
Total Held to Maturity Securities	**$ 114,415**	**$ 1,220**	**$ (188)**	**$ 115,447**

September 30, 2018 (In thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Mortgage-backed securities- U.S. Government Sponsored Enterprises (GSE'S)	$ 86,723	$ 203	$ (2,564)	$ 84,362
Collateralized mortgage obligations	1,173	38	-	1,211
Municipal bonds	9,955	296	(157)	10,094
U.S. Government Agencies	9,191	-	(912)	8,279
Total Held to Maturity Securities	$ 107,042	$ 537	$ (3,633)	$ 103,946

All the Company's mortgage-backed securities and collateralized mortgage obligations are residential. At September 30, 2019, the Bank held $1.1 million in Collateralized Mortgage Obligations (CMOs) of which all were issued by Government Sponsored Enterprises and none were privately issued.

Proceeds from the sales of held-to-maturity mortgage-backed securities during the year ended September 30, 2019 were $3.6 million with a related gross realized gain of $144,000. At the time of sale, all of the mortgage-backed securities had been paid down at least 85% of their acquired par.

There were no sales of securities during the year ended September 30, 2018.

A summary of securities with unrealized losses, aggregated by category, as of September 30, 2019 and September 30, 2018 is as follows:

	September 30, 2019					
	Less than 12 Months		12 Months or Longer			
(In thousands)	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Total Fair Value	Total Unrealized Losses
Mortgage-backed securities- U.S. Government Sponsored Enterprises (GSE'S)	$ 17,228	$ (104)	$ 9,808	$ (79)	$ 27,039	$ (183)
Collateralized mortgage obligations	118	(1)	-	-	118	(1)
U.S. Government Agencies	4,192	(4)	-	-	4,192	(4)
Total temporarily impaired securities	$ 21,538	$ (109)	$ 9,808	$ (79)	$ 31,346	$ (188)

	September 30, 2018					
	Less than 12 Months		12 Months or Longer			
(In thousands)	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Total Fair Value	Total Unrealized Losses
Mortgage-backed securities- U.S. Government Sponsored Enterprises (GSE'S)	$ 44,496	$ (991)	$ 32,912	$ (1,573)	$ 77,408	$ (2,564)
Municipal bonds	2,943	(113)	662	(44)	3,605	(157)
U.S. Government Agencies	1,146	(48)	7,133	(864)	8,279	(912)
Total temporarily impaired securities	$ 48,585	$ (1,152)	$ 40,707	$ (2,481)	$ 89,292	$ (3,633)

At September 30, 2019, debt securities in a gross unrealized loss position consisted of 29 securities that at such date had an aggregate depreciation of 0.6% from the Company's amortized cost basis. Management believes that the estimated fair value of the securities disclosed above is primarily dependent upon the movement in market interest rates. Management evaluated the length of time and the extent to which the fair value has been less than cost; the financial condition and near term prospects of the issuer, including any specific events which may influence the operations of the issuer. The Company has the ability and intent to hold these securities until maturity and the Company does not believe it will be required to sell such securities prior to the recovery of the amortized cost basis. Management does not believe any individual unrealized loss on debt securities as of September 30, 2019 represents other-than-temporary impairment.

The following table sets forth the stated maturities of the investment and mortgage-backed securities at September 30, 2019. Money market funds are not included in the table based on lack of maturity.

	September 30, 2019	
(In thousands)	Amortized Cost	Fair Value
Available for sale:		
Due after ten years	$ 765	$ 778
Total	$ 765	$ 778
Held to maturity:		
Due after one year through five years	$ 15,859	$ 15,981
Due after five years through ten years	37,649	38,039
Due after ten years	60,907	61,427
Total	$ 114,415	$ 115,447

Certain of the Company's investment securities, totaling $33.4 million and $41.0 million at September 30, 2019 and 2018, respectively, were pledged or restricted for deposit sweep accounts, public deposits, or other purposes as required or permitted by law.

4. LOANS RECEIVABLE

Loans receivable consists of the following:

	September 30,	
(In thousands)	**2019**	**2018**
Residential Mortgages	**$ 325,126**	$ 327,587
Construction	**4,223**	7,767
Home Equity	**74,487**	85,749
Commercial Mortgages	**202,749**	197,373
Commercial Business Loans	**4,614**	5,128
Consumer Non-Real Estate	**444**	385
Total	**611,643**	623,989
Undisbursed portion of loans in process	**(2,168)**	(4,226)
Deferred loan fees	**66**	58
Allowance for loan losses	**(4,757)**	(3,922)
Loans Receivable - net	**$ 604,784**	$ 615,899

At September 30, 2019 and 2018, the Company was servicing residential mortgage loans for others amounting to approximately $12.0 million and $13.0 million, respectively. Servicing loans for others generally consists of collecting mortgage payments, maintaining escrow accounts, disbursing payments to investors and foreclosure processing. Loan servicing income is recognized over the life of the loan. The Company receives a servicing fee of 0.25% on sold loans, which totaled $37,000 as of September 30, 2019. These servicing fees are included in prepaid expenses and other assets on the Consolidated Statements of Financial Condition. In connection with the loans serviced for others, the Company held borrowers' escrow balances of approximately $55,000 and $51,000 at September 30, 2019 and 2018, respectively.

The Bank has had, and may be expected to have in the future, loan transactions in the ordinary course of business with directors, officers, principal stockholders, their immediate families and affiliated companies (commonly referred to as related parties), on the same terms including interest rates and collateral, as those prevailing at the time for comparable transactions with others. Loans to related parties at September 30, 2019 and 2018, were approximately $13.7 million and $14.1 million, respectively. There were no additional loans for the year ended September 30, 2019 and repayments were $406,000 compared to $12.4 million in additional loans and $580,000 in repayments for the year ended September 30, 2018.

The loans receivable portfolio is segmented into consumer and commercial loans. Consumer loans consist of the following classes: residential mortgage loans, construction loans, home equity loans and non-real estate consumer loans. Commercial loans consist of the following classes: commercial mortgages and commercial business loans. For all classes of loans receivable, the accrual of interest is discontinued when the contractual payment of principal or interest has become 90 days past due or management has serious doubts about further collectability of principal or interest, even though the loan is currently performing. A loan may remain on accrual status if it is in the process of collection and is either guaranteed or well secured. When a loan is placed on nonaccrual status, unpaid interest credited to income in the current year is reversed and unpaid interest accrued in prior years is charged against the allowance for loan losses. Interest received on nonaccrual loans including impaired loans generally are either applied against principal or reported as interest income, according to management's judgment as to the collectability of principal. Generally, loans are restored to accrual status when the obligation is brought current, has performed in accordance with the contractual terms for a reasonable period of time (generally six months) and the ultimate collectability of the total contractual principal and interest is no longer in doubt. The past due status of all classes of loans receivable is determined based on contractual due dates for loan payments.

The allowance for loan losses represents management's estimate of losses inherent in the loan portfolio as of the Consolidated Statements of Financial Condition date and is recorded as a reduction to loans. The allowance for loan losses is increased by the provision for loan losses, and decreased by charge-offs, net of recoveries. Loans deemed to be uncollectible are charged against the allowance for loan losses, and subsequent recoveries, if any, are credited to the allowance. All, or part, of the principal balance of loans receivable are charged off to the allowance as soon as it is determined that the repayment of all, or part, of the principal balance is highly unlikely. Because all identified losses are immediately charged off, no portion of the allowance for loan losses is restricted to any individual loan or groups of loans, and the entire allowance is available to absorb any and all loan losses.

The allowance for loan losses is maintained at a level considered adequate to provide for losses that can be reasonably anticipated. Management performs a monthly evaluation of the adequacy of the allowance. The allowance is based on the Company's past loan loss experience, known and inherent risks in the portfolio, adverse situations that may affect the borrower's ability to repay, the estimated value of any underlying collateral, composition of the loan portfolio, current economic conditions and other relevant factors. This evaluation is inherently subjective as it requires material estimates that may be susceptible to significant revision as more information becomes available.

The allowance consists of specific, general and unallocated components. The specific component relates to loans that are classified as impaired. For loans that are classified as impaired, an allowance is established when the discounted cash flows (or collateral value or observable market price) of the impaired loan is lower than the carrying value of that loan. The general component covers pools of loans by loan class. These pools of loans are evaluated for loss exposure based upon historical loss rates for each of these categories of loans, adjusted for qualitative factors. These significant factors may include changes in lending policies and procedures, changes in existing general economic and business conditions affecting our primary lending areas, credit quality trends, collateral value, loan volumes and concentrations, seasoning of the loan portfolio, recent loss experience in particular segments of the portfolio, duration of the current business cycle and bank regulatory examination results. The applied loss factors are reevaluated quarterly to ensure their relevance in the current economic environment.

Residential mortgage lending generally entails a lower risk of default than other types of lending. Other consumer loans and commercial real estate loans generally involve more risk of collectability because of the type and nature of the collateral and, in certain cases, the absence of collateral. It is the Company's policy to establish specific reserves for losses on delinquent commercial loans when it determines that losses are probable.

An unallocated component is maintained to cover uncertainties that could affect management's estimate of probable losses. The unallocated component of the allowance reflects the margin of imprecision inherent in the underlying assumptions used in the methodologies for estimating specific and general losses in the portfolio.

A loan is considered impaired when, based on current information and events, it is probable that the Company will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Additionally, all loans modified in a troubled debt restructuring are considered impaired. Factors considered by management in determining impairment include payment status, collateral value and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record and the amount of the shortfall in relation to the principal and interest owed. Impairment is measured on a loan by loan basis for loans by either the present value of expected future cash flows discounted at the loan's effective interest rate or the fair value of the collateral if the loan is collateral dependent.

An allowance for loan losses is established for an impaired loan if its carrying value exceeds its estimated fair value. The estimated fair values of substantially all of the Company's impaired loans are measured based on the estimated fair value of the loan's collateral. Interest payments on impaired loans and non-accrual loans are applied to principal unless the ability to collect the principal amount is fully secured, in which case interest is recognized on the cash basis.

For residential mortgage loans, home equity loans and commercial loans secured by real estate, estimated fair values are determined primarily through third-party appraisals. When a real estate secured loan becomes impaired, a decision is made regarding whether an updated certified appraisal of the real estate is necessary. This decision is based on various considerations, including the age of the most recent appraisal, the loan-to-value ratio based on the original appraisal and the condition of the property. Appraised values are discounted to arrive at the estimated selling price of the collateral, which is considered to be the estimated fair value. The discounts also include estimated costs to sell the property.

For commercial business loans secured by non-real estate collateral, such as accounts receivable, inventory and equipment, estimated fair values are determined based on the borrower's financial statements, inventory reports, accounts receivable aging or equipment appraisals or invoices. Indications of value from these sources are generally discounted based on the age of the financial information or the quality of the assets.

The allowance calculation methodology includes further segregation of loan classes into risk rating categories. The borrower's overall financial condition, repayment sources, guarantors and value of collateral, if appropriate, are evaluated annually for commercial loans or when credit deficiencies arise, such as delinquent loan payments, for commercial and consumer loans. Credit quality risk ratings include regulatory classifications of special mention, substandard, doubtful and loss. Loans criticized special mention have potential weaknesses that deserve management's close attention. If uncorrected, the potential weaknesses may result in deterioration of the repayment prospects. Loans classified substandard have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They include loans that are inadequately protected by the current sound net worth and paying capacity of the obligor or of the collateral pledged, if any. Loans classified doubtful have all the weaknesses inherent in loans classified substandard with the added characteristic that collection or liquidation in full, on the basis of current conditions and facts, is highly improbable. Loans classified as a loss are considered uncollectible and are charged to the allowance for loan losses. Loans not classified are rated pass.

In addition, federal regulatory agencies, as an integral part of their examination process, periodically review the Company's allowance for loan losses and may require the Company to recognize additions to the allowance based on their judgments about information available to them at the time of their examination, which may not be currently available to management. Based on management's comprehensive analysis of the loan portfolio, management believes the current level of the allowance for loan losses is adequate.

The following table presents the classes of the loan portfolio summarized by the aggregate pass rating and the classified ratings of special mention, substandard and doubtful within the Company's internal risk rating system as of September 30, 2019 and 2018:

September 30, 2019

(In thousands)	Pass	Special Mention	Substandard	Doubtful	Total
Residential Mortgages	**$ 320,469**	**$ 79**	**$ 4,578**	**$ -**	**$ 325,126**
Construction	**4,223**	**-**	**-**	**-**	**4,223**
Home Equity	**73,824**	**16**	**647**	**-**	**74,487**
Commercial Mortgages	**196,987**	**1,306**	**4,456**	**-**	**202,749**
Commercial Business Loans	**4,374**	**90**	**150**	**-**	**4,614**
Consumer Non-Real Estate	**444**	**-**	**-**	**-**	**444**
Total	**$ 600,321**	**$ 1,491**	**$ 9,831**	**$ -**	**$ 611,643**

September 30, 2018

(In thousands)	Pass	Special Mention	Substandard	Doubtful	Total
Residential Mortgages	$ 322,342	$ 182	$ 4,283	$ 780	$ 327,587
Construction	7,767	-	-	-	7,767
Home Equity	85,327	16	271	135	85,749
Commercial Mortgages	191,678	1,177	4,518	-	197,373
Commercial Business Loans	4,833	92	203	-	5,128
Consumer Non-Real Estate	385	-	-	-	385
Total	$ 612,332	$ 1,467	$ 9,275	$ 915	$ 623,989

The following table summarizes information in regards to impaired loans by loan portfolio class as of September 30, 2019 and for the year then ended:

(In thousands)	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
With no related allowance recorded:					
Residential Mortgages	$ 4,206	$ 4,268	$ -	$ 4,335	$ 219
Construction	-	-	-	-	-
Home Equity	342	496	-	500	18
Commercial Mortgages	4,456	4,664	-	4,697	91
Commercial Business Loans	150	150	-	150	9
Consumer Non-Real Estate	-	-	-	-	-
Subtotal:	9,154	9,578	-	9,682	337
With an allowance recorded:					
Residential Mortgages	372	372	(5)	379	23
Construction	-	-	-	-	-
Home Equity	347	347	(213)	348	21
Commercial Mortgages	-	-	(223)	-	-
Commercial Business Loans	-	-	-	-	-
Consumer Non-Real Estate	-	-	-	-	-
Subtotal:	719	719	(441)	727	44
Total:					
Residential Mortgages	4,578	4,640	(5)	4,714	242
Construction	-	-	-	-	-
Home Equity	689	843	(213)	848	39
Commercial Mortgages	4,456	4,664	(223)	4,697	91
Commercial Business Loans	150	150	-	150	9
Consumer Non-Real Estate	-	-	-	-	-
Totals:	$ 9,873	$ 10,297	$ (441)	$ 10,409	$ 381

The following table summarizes information in regards to impaired loans by loan portfolio class as of September 30, 2018 and for the year then ended:

(In thousands)	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
With no related allowance recorded:					
Residential Mortgages	$ 4,530	$ 4,591	$ -	$ 4,461	$ 165
Construction	-	-	-	-	-
Home Equity	212	367	-	260	11
Commercial Mortgages	4,518	4,726	-	4,549	96
Commercial Business Loans	150	150	-	150	8
Consumer Non-Real Estate	-	-	-	-	-
Subtotal:	9,410	9,834	-	9,420	280
With an allowance recorded:					
Residential Mortgages	533	533	(24)	539	25
Construction	-	-	-	-	-
Home Equity	194	194	(124)	197	9
Commercial Mortgages	-	-	-	-	-
Commercial Business Loans	53	274	(12)	275	-
Consumer Non-Real Estate	-	-	-	-	-
Subtotal:	780	1,001	(160)	1,011	34
Total:					
Residential Mortgages	5,063	5,124	(24)	5,000	190
Construction	-	-	-	-	-
Home Equity	406	561	(124)	457	20
Commercial Mortgages	4,518	4,726	-	4,549	96
Commercial Business Loans	203	424	(12)	425	8
Consumer Non-Real Estate	-	-	-	-	-
Totals:	$ 10,190	$ 10,835	$ (160)	$ 10,431	$ 314

The performance and credit quality of the loan portfolio is also monitored by the analyzing the age of the loans receivable as determined by the length of time a recorded payment is past due. The following tables present the classes of the loan portfolio summarized by the past due status as of September 30, 2019 and 2018:

September 30, 2019

(In thousands)	30-89 Days Past Due	Greater than 90 Days	Total Past Due	Current	Total Loans Receivable	Loans Receivable > 90 Days and Accruing
Residential Mortgages	$ 3,632	$ 1,938	$ 5,570	$319,556	$ 325,126	$ -
Construction	-	-	-	4,223	4,223	-
Home Equity	1,525	327	1,852	72,635	74,487	-
Commercial Mortgages	-	4,008	4,008	198,741	202,749	-
Commercial Business Loans	-	-	-	4,614	4,614	-
Consumer Non-Real Estate	47	-	47	397	444	-
Total	$ 5,204	$ 6,273	$ 11,477	$600,166	$ 611,643	$ -

September 30, 2018

(In thousands)	30-89 Days Past Due	Greater than 90 Days	Total Past Due	Current	Total Loans Receivable	Loans Receivable > 90 Days and Accruing
Residential Mortgages	$ 4,264	$ 3,922	$ 8,186	$319,401	$ 327,587	$ -
Construction	-	-	-	7,767	7,767	-
Home Equity	911	361	1,272	84,477	85,749	-
Commercial Mortgages	-	4,518	4,518	192,855	197,373	-
Commercial Business Loans	25	203	228	4,900	5,128	-
Consumer Non-Real Estate	-	-	-	385	385	-
Total	$ 5,200	$ 9,004	$ 14,204	$609,785	$ 623,989	$ -

The following table presents nonaccrual loans by classes of the loan portfolio for the years ended September 30, 2019 and 2018:

	September 30, 2019	September 30, 2018
(In thousands)		
Residential Mortgages	**$ 4,578**	$ 4,482
Construction	**-**	-
Home Equity	**647**	361
Commercial Mortgages	**4,008**	4,518
Commercial Business Loans	**-**	203
Consumer Non-Real Estate	**-**	-
Total	**$ 9,233**	$ 9,564

The following table provides the activity in the allowance for loan losses by loan class for the years ended September 30, 2019 and 2018 and the balance in the allowance for loan losses at September 30, 2019 and 2018 disaggregated on the basis of the Company's impairment method by loan class along with the balance of loans receivable by class disaggregated on the basis of the Company's impairment methodology.

	September 30, 2019							
(In thousands)	Residential Mortgages	Construction	Home Equity	Commercial Mortgages	Commercial Business Loans	Consumer Non-Real Estate	Unallocated	Totals
Allowance for loan loss:								
Beginning Balance, September 30, 2018	$ 1,040	$ -	$ 519	$ 1,569	$ 170	$ 24	$ 600	$ 3,922
Charge-offs	(64)	-	(6)	-	(54)	(30)	-	(154)
Recoveries	-	-	-	-	-	7	-	7
Provisions	(65)	-	(2)	495	31	33	490	982
Ending balance, September 30, 2019	$ 911	$ -	$ 511	$ 2,064	$ 147	$ 34	$ 1,090	$ 4,757
Ending balance:								
Individually evaluated for impairment	$ 5	$ -	$ 213	$ 223	$ -	$ -	$ -	$ 441
Ending balance:								
Collectively evaluated for impairment	$ 906	$ -	$ 298	$ 1,841	$ 147	$ 34	$ 1,090	$ 4,316
Loans:								
Ending balance:	$ 325,126	$ 4,223	$ 74,487	$ 202,749	$ 4,614	$ 444	$ -	$611,643
Ending balance:								
Individually evaluated for impairment	$ 4,578	$ -	$ 689	$ 4,456	$ 150	$ -	$ -	$ 9,873
Ending balance:								
Collectively evaluated for impairment	$ 320,548	$ 4,223	$ 73,798	$ 198,293	$ 4,464	$ 444	$ -	$601,770

During the fiscal year ended September 30, 2019 a credit provision was recorded in the residential mortgage and home equity portfolios while the commercial mortgage, commercial business loan and consumer non-real-estate portfolios required provision expense. The credit provision in the residential mortgage and home equity portfolios was the result of decreased historical loss factors. The provision expense recorded for the commercial mortgage, commercial business loan and consumer non-real-estate portfolios was the result of increased historical loss factors, no qualitative factor changes occurred in fiscal year 2019.

(In thousands)	Residential Mortgages	Construction	Home Equity	Commercial Mortgages	Commercial Business Loans	Consumer Non-Real Estate	Unallocated	Totals
	September 30, 2018							
Allowance for loan loss:								
Beginning Balance, September 30, 2017	$ 1,235	$ -	$ 549	$ 1,382	$ 128	$ 19	$ 750	$ 4,063
Charge-offs	(30)	-	-	(75)	(1,023)	(59)	-	(1,187)
Recoveries	-	-	-	-	-	6	-	6
Provisions	(165)	-	(30)	262	1,065	58	(150)	1,040
Ending balance, September 30, 2018	$ 1,040	$ -	$ 519	$ 1,569	$ 170	$ 24	$ 600	$ 3,922
Ending balance:								
Individually evaluated for impairment	$ 24	$ -	$ 124	$ -	$ 12	$ -	$ -	$ 160
Ending balance:								
Collectively evaluated for impairment	$ 1,016	$ -	$ 395	$ 1,569	$ 158	$ 24	$ 600	$ 3,762
Loans:								
Ending balance:	$ 327,587	$ 7,767	$ 85,749	$ 197,373	$ 5,128	$ 385	$ -	$623,989
Ending balance:								
Individually evaluated for impairment	$ 5,063	$ -	$ 406	$ 4,518	$ 203	$ -	$ -	$ 10,190
Ending balance:								
Collectively evaluated for impairment	$ 322,524	$ 7,767	$ 85,343	$ 192,855	$ 4,925	$ 385	$ -	$613,799

During the fiscal year ended September 30, 2018 a credit provision was recorded in the residential mortgage and home equity portfolios while the commercial mortgage, commercial business loan and consumer non-real-estate portfolios required provision expense. The credit provision in the residential mortgage and home equity portfolios was the result of decreased qualitative factors. The provision expense recorded for the commercial mortgage, commercial business loan and consumer non-real-estate portfolios was the result of increased historical loss factors and qualitative factors.

Foreclosed assets acquired in settlement of loans are carried at fair value, less estimated costs to sell. As of September 30, 2019, included within the foreclosed assets are no consumer residential mortgages on or received via a deed in lieu transaction prior to the period end. As of September 30, 2019, the Company has initiated formal foreclosure proceeds on $1.5 million of consumer residential mortgages loans, which have not yet been transferred into foreclosed assets.

A troubled debt restructuring (“TDR”) is a formal restructure of a loan when the lender, for economic or legal reasons related to the borrower’s financial difficulties, grants a concession to the borrower. The concessions may be granted in various forms, including reduction in the stated interest rate, reduction in the loan balance or accrued interest, or extension of the maturity date.

The following table summarizes information in regards to troubled debt restructurings for the twelve months ended September 30, 2019 (in thousands):

Troubled Debt Restructurings	Number of Contracts	Pre-Modification Outstanding Recorded Investments	Post-Modification Outstanding Recorded Investments
Residential mortgage	1	171	171
Totals	1	$ 171	$ 171

As indicated in the table above, the Company modified one residential mortgage loan with a recorded investment of $171,000 during the twelve months ended September 30, 2019. As a result of the modification the Company modified the interest rate on the loan. The effective interest rate of the new term of the modified loan was reduced when compared to the interest rate of the original term of the modified loan.

For the year ended September 30, 2019 there were no loan modifications classified as troubled debt restructuring that subsequently defaulted within one year of modification.

The following table summarizes information in regards to troubled debt restructurings for the twelve months ended September 30, 2018 (in thousands):

Troubled Debt Restructurings	Number of Contracts	Pre-Modification Outstanding Recorded Investments	Post-Modification Outstanding Recorded Investments
Home equity	1	46	46
Totals	1	$ 46	$ 46

As indicated in the table above, the Company modified one home equity loan with a recorded investment of $46,000 during the twelve months ended September 30, 2018. As a result of the modification the Company added uncollected overdue amounts to the principal balance of the loan, which are due at maturity.

For the year ended September 30, 2018 there were no loan modifications classified as troubled debt restructuring that subsequently defaulted within one year of modification.

5. OFFICE PROPERTIES AND EQUIPMENT

Office properties and equipment are summarized by major classifications as follows:

	September 30,	
(In thousands)	2019	2018
Land	$ 3,277	$ 3,277
Buildings	10,622	10,562
Fixed assets suspense	146	-
Furniture, fixtures and equipment	5,965	5 ,908
Data processing	2,134	2,021
Automobiles	82	82
Total	22,226	21,850
Less accumulated depreciation	(11,941)	(11,219)
Net	$10,285	$ 10,631

Depreciation expense for the years ended September 30, 2019 and 2018 amounted to approximately $722,000 and $739,000, respectively.

6. DEPOSITS

Deposits are summarized as follows:

	September 30,			
	2019		2018	
(In thousands)	Amount	Weighted Average Interest Rate	Amount	Weighted Average Interest Rate
Non-interest-bearing checking accounts	$ 60,602	0.00%	$ 55,537	0.00%
NOW accounts	43,735	0.04	41,553	0.04
Interest-bearing checking accounts	76,717	0.68	75,341	0.63
Money market deposit accounts	205,779	0.32	217,177	0.30
Passbook and club accounts	2,854	0.70	2,982	0.71
Certificate of deposit accounts	196,655	1.86	189,488	1.57
Total Deposits	$586,342	0.83%	$582,078	0.71%

At September 30, 2019, the amounts of scheduled maturities of certificate of deposit accounts were as follows (in thousands):

For the year ended September 30,	2020	$ 89,375
	2021	48,394
	2022	48,470
	2023	6,735
	2024	3,681
Total		$ 196,655

The aggregate amount of certificate accounts in denominations of $250,000 or more at September 30, 2019 and 2018 amounted to approximately $15.2 million and $16.8 million, respectively.

7. SHORT-TERM BORROWINGS AND LONG-TERM DEBT

The Bank's short-term borrowings activities are summarized as follows:

FHLB RepoPlus Advance	**2019**	**2018**
	(Dollar in thousands)	
Balance at year-end	**$ 8,830**	$17,207
Maximum amount of outstanding at any month-end	**20,222**	18,099
Average balance outstanding during the year	**11,391**	14,773
Weighted-average interest rate:		
As of year-end	**0.51%**	0.61%
Paid during the year	**0.86%**	0.72%

Average amounts outstanding during the year represent daily average balances, while weighted-average interest rates represent interest expense divided by the related average balance for the period indicated.

The Bank maintains the Repo Plus Advance credit arrangement, which is renewable annually, with the FHLB. The line maintains a variable rate of interest that may be reset daily at the FHLB's discretion. The Bank's maximum borrowing capacity under the credit arrangement with the FHLB as of September 30, 2019, is approximately $398.0 million. FHLB advances are secured by a blanket security agreement that includes the Company's FHLB stock as well as certain residential mortgage loans and investments.

Long-term debt consists of the following (in thousands):

	Maturity Range		**Weighted Average Interest**	**Stated Interest Rate Range**			
Description	**From**	**To**	**Rate**	**From**	**To**	**2019**	**2018**
Fixed rate	12/16/2019	01/31/2025	2.41%	1.64%	3.25%	**$ 89,295**	$ 78,309
Convertible	03/23/2020	10/19/2020	1.86%	1.73%	2.01%	**13,000**	13,000
						$102,295	$91,309

Maturities of long-term advances as of September 30, 2019 are summarized as follows:

		Amount	Weighted Average Rate
		(In thousands)	
FHLB long-term debt:			
	2020	$ 14,034	1.85%
	2021	21,261	2.12%
	2022	12,000	2.20%
	2023	38,000	2.47%
	2024	11,000	2.84%
	Thereafter	6,000	2.81%
Total FHLB long-term debt		102,295	2.34%

8. INCOME TAXES

The Company computes its reserve for bad debts under the specific charge-off method. The bad debt deduction allowable under this method is available to large banks with assets greater than $500 million. Generally, this method allows the Company to deduct an annual addition to the reserve for bad debts equal to its net charge-offs. Retained earnings at September 30, 2019 and 2018 includes approximately $1,325,000 representing bad debt deductions for which no deferred income taxes have been provided.

The expense for income taxes differs from that computed at the statutory federal corporate tax rate as follows:

	Year Ended September 30,			
	2019		2018	
(In thousands)	Amount	Percentage of Pretax Income	Amount	Percentage of Pretax Income
At statutory rate	$ 2,355	21.0%	$ 2,422	24.3%
Adjustments resulting from:				
Tax-exempt income	(159)	(1.4)	(196)	(2.0)
State tax-net of federal tax benefit	712	6.3	395	4.0
Change in corporate rate tax	-	-	355	3.6
Other	156	1.4	(98)	(1.0)
Expense per consolidated statements of income	$ 3,064	27.3%	$ 2,879	28.8%

Income tax expense is summarized as follows:

	Year Ended September 30,	
(In thousands)	2019	2018
Current	$ 3,156	$ 2,542
Deferred	(92)	(18)
Change in corporate tax rate	-	355
Total Income Tax Expense	$ 3,064	$ 2,879

Items that gave rise to significant portions of the deferred tax accounts are as follows:

(In thousands)	September 30, 2019	2018
Deferred Tax Assets:		
Deferred Loan Fees	**$ 23**	$ 12
Allowance for Loan Losses	**999**	824
Other	**313**	389
Sub-Total	**1,335**	1,225
Deferred Tax Liabilities:		
Unrealized gain on investment securities	**(4)**	(4)
Properties and equipment	**(652)**	(634)
Sub-Total	**(656)**	(638)
Total	**$ 679**	$ 587

9. REGULATORY CAPITAL REQUIREMENTS

The Bank is subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the Bank's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Bank must meet specific capital guidelines that involve quantitative measures of the Bank's assets, liabilities, and certain off-balance-sheet items as calculated under U.S. GAAP, regulatory reporting requirements, and regulatory capital standards. The Bank's capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

Quantitative measures established by regulatory capital standards to ensure capital adequacy require the Bank to maintain minimum amounts and ratios (set forth in the following table) of total and Tier 1 capital to risk-weighted assets, common equity Tier 1 capital to total risk-weighted assets, and of Tier 1 capital to average assets. Management believes, as of September 30, 2019, that the Bank meets all capital adequacy requirements to which it is subject.

As of September 30, 2019, and September 30, 2018, the most recent notification from the Federal Deposit Insurance Corporation categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized the Bank must maintain minimum total risk-based capital, Tier 1 risk-based capital, common equity Tier 1 risk-based capital, and Tier 1 leverage ratios as set forth in the table. There are no conditions or events since that notification that management believes have changed the institution's category.

The Bank's actual capital amounts and ratios are also presented in the table.

(In thousands)	Actual		For Capital Adequacy Purposes		To Be Considered Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
At September 30, 2019						
Tier 1 Capital (to assets)	**$76,253**	**9.72%**	**$31,373**	**4.00%**	**$39,216**	**5.00%**
Common Equity Tier 1 Capital (to risk weighted assets)	**76,253**	**14.00%**	**24,511**	**4.50%**	**35,404**	**6.50%**
Tier 1 Capital (to risk weighted assets)	**76,253**	**14.00%**	**32,681**	**6.00%**	**43,574**	**8.00%**
Total Capital (to risk weighted assets)	**81,095**	**14.89%**	**43,574**	**8.00%**	**54,468**	**10.00%**
At September 30, 2018						
Tier 1 Capital (to assets)	$71,901	9.26%	$31,072	4.00%	$38,840	5.00%
Common Equity Tier 1 Capital (to risk weighted assets)	71,901	13.02%	24,846	4.50%	35,889	6.50%
Tier 1 Capital (to risk weighted assets)	71,901	13.02%	33,128	6.00%	44,171	8.00%
Total Capital (to risk weighted assets)	75,907	13.75%	44,171	8.00%	55,214	10.00%

The Company's capital ratios are not significantly different than the Bank's disclosed above.

10. RETIREMENT SAVINGS PLANS

The Company has a qualified 401 (k) retirement savings plan covering all full-time employees meeting certain eligibility requirements. Contributions for the plan are at the discretion of the Company's Board of Directors. Compensation expense related to the plan was $550,000 and $536,000 for the years ended September 30, 2019 and 2018, respectively.

11. STOCK BASED COMPENSATION AND EMPLOYEE STOCK PURCHASE PLAN

In January 2016, the stockholders approved the 2015 Stock Incentive Plan which provides 300,000 shares for the granting of incentive stock options, compensatory stock options, stock appreciation rights and share awards of restrictive stock. The number of shares available to be issued as share awards will not exceed 75,000 shares. There are 142,387 shares remaining for grant under this plan.

The life of the options under the above plan is ten years. The vesting period for the options is between one and five years.

A summary of stock option transactions under these plans follows:

	2019		2018	
	Options	Weighted Average Price	Options	Weighted Average Price
Outstanding, beginning of year	**357,235**	**$ 18.13**	334,848	$ 16.17
Exercised	**(54,682)**	**14.21**	(55,812)	13.59
Forfeited	**(9,650)**	**18.97**	(2,400)	19.77
Expired	**-**	**-**	-	-
Granted	**34,354**	**23.70**	80,599	23.20
Outstanding, end of year	**327,257**	**$ 19.35**	357,235	$ 18.13
Options exercisable, end of year	**164,207**	**$ 17.85**	181,513	$ 15.89

A summary of the exercise price ranges at September 30, 2019 and 2018 is as follows:

2019

Number of Option Shares	Exercise Price Range	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price per Share
87,022	**$ 11.90-16.95**	**2.90**	**$ 15.61**
128,682	**16.96-18.80**	**5.40**	**18.40**
111,553	**18.81-24.55**	**8.82**	**23.36**
327,257	**$11.90-24.55**	**5.90**	**$ 19.35**

2018

Number of Option Shares	Exercise Price Range	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price per Share
76,196	$ 11.85-14.84	2.10	$ 13.93
116,519	14.85-18.50	4.50	16.98
164,520	18.51-24.55	8.42	20.90
357,235	$11.85-24.55	5.79	$ 18.13

At September 30, 2019 and 2018, the aggregate intrinsic value of options outstanding was $1.2 million and $2.0 million, respectively. At September 30, 2019 and 2018, the aggregate intrinsic value of options exercisable was $835,000 and $1.4 million, respectively. For the years ended September 30, 2019 and 2018, the aggregate intrinsic value of options exercised was $674,000 and $437,000, respectively.

The aggregate intrinsic value of a stock option represents the total pre-tax intrinsic value (the amount by which the current market value of the underlying stock exceeds the exercise price of the option) that would have been received by the option holder had all option holders exercised their options on September 30, 2019. This amount changes based on changes in the market value of the Company's common stock.

The weighted average fair value of stock options granted in the years ended September 30, 2019 and 2018 was $3.93 and $4.34, respectively, and was estimated at the date of grant using a Binomial Option Pricing Model with the following weighted-average assumptions while the market price of the Company's common stock at the date of grant is used for restricted stock awards:

	Year Ended September 30,	
	2019	**2018**
Risk free interest rate of return	**1.54%**	2.49%
Expected option life	**84 months**	84 months
Expected volatility	**23.00%**	23.50%
Expected dividends	**4.22%**	3.80%

The expected volatility is based on historic volatility. The risk-free interest rates for periods within the contractual life of the awards are based on the U.S. Treasury yield curve in effect at the time of the grant. The expected life is based on historical exercise experience. The dividend yield assumption is based on the Company's history and expectation of dividend payouts.

Stock based compensation expense related to stock options for the years ended September 30, 2019 and 2018 was $216,000 or $197,000 net of tax, and $156,000 or $147,000 net of tax, respectively. As of September 30, 2019, there was approximately $149,000 of total unrecognized compensation cost related to non-vested stock options under the plans.

On November 8, 2016, 4,802 shares of restricted stock were awarded. The restricted shares awarded had a grant date fair value of $18.66 per share. The restricted stock awarded vests 33% annually beginning November 8, 2017. On November 7, 2017, 4,474 shares of restricted stock were awarded. The restricted shares awarded had a grant date fair value of $22.00 per share. The restricted stock awarded vests 33% annually beginning November 7, 2018. On August 15, 2018, 3,085 shares of restricted stock were awarded. The restricted shares awarded had a grant date fair value of $24.55 per share. The restricted stock awarded vests 33% annually beginning August 15, 2019. On August 20, 2019, 3,334 shares of restricted stock were awarded. The restricted shares awarded had a grant date fair value of $23.70 per share. The restricted stock awarded vests 33% annually beginning August 20, 2020. During the years ended September 30, 2019 and 2018, $93,000 and $102,000, respectively in compensation expense was recognized in regard to these restricted stock awards. At September 30, 2019, there was $111,000 of unrecognized compensation expense related to the restricted stock awards which is expected to be recognized over a period of three years.

Restricted stock award activity for the year ended September 30, 2019 was as follows:

	Number of shares	Weighted Average Grant Date Fair Value
Unvested restricted stock, beginning of year	**12,311**	**$ 21.37**
Granted	**3,334**	**23.70**
Forfeited	**-**	**-**
Vested	**(5,670)**	**20.64**
Unvested restricted stock, end of year	**9,975**	**$ 22.56**

Restricted stock award activity for the year ended September 30, 2018 was as follows:

	Number of shares	Weighted Average Grant Date Fair Value
Unvested restricted stock, beginning of year	9,558	$ 18.41
Granted	7,559	23.04
Forfeited	-	-
Vested	(4,806)	18.11
Unvested restricted stock, end of year	12,311	$ 21.37

The Company also has established an Employee Stock Purchase Plan (the "Purchase Plan") whereby employees may elect to make contributions to the Purchase Plan in an aggregate amount not less than 2% or more than 10% of such employee's total compensation. These contributions would then be used to purchase stock during an offering period determined by the Company's Salary and Benefits Committee. The purchase price of the stock would be the lesser of 85% of the market price on the first day or the last day of the offering period. At September 30, 2019 and 2018, there were 53,583 shares available for future purchase. The Company suspended participation in the Purchase Plan in March 2005 and the plan is not currently active.

12. ACCUMULATED OTHER COMPREHENSIVE INCOME

The following table presents the changes in accumulated other comprehensive income by component net of tax for the years ended September 30, 2019 and 2018.

	Unrealized gains on available for sale securities (a) (In thousands)
Balance as of September 30, 2018	**$ 11**
Other comprehensive loss before reclassification	**(4)**
Amount reclassified from accumulated other comprehensive income	**-**
Total other comprehensive loss	**(4)**
Balance as of September 30, 2019	**$ 7**

(a) All amounts are net of tax. Amounts in parentheses indicate debits.

	Unrealized gains on available for sale securities (a) (In thousands)
Balance as of September 30, 2017	$ 13
Other comprehensive loss before reclassification	(4)
Amount reclassified from accumulated other comprehensive income	-
Reclassified of certain income tax effect from accumulated other comprehensive income	2
Total other comprehensive loss	(2)
Balance as of September 30, 2018	$ 11

(a) All amounts are net of tax. Amounts in parentheses indicate debits.

There were no items that were reclassified from accumulated other comprehensive income for the years ended September 30, 2019 and 2018.

13. COMMITMENTS

At September 30, 2019, the Company had approximately $8.5 million in outstanding commitments to originate mortgage loans, of which $7.2 million were fixed rates ranging from 3.38% to 5.50% and $1.3 million were adjustable rates ranging from 3.50% to 4.75%. The unfunded home equity line of credit commitments at September 30, 2019 were $65.6 million. The Company had $899,000 and $1.4 million of committed commercial and consumer loans, respectively, at September 30, 2019. In addition, the Company had $20.8 million of unused commercial lines of credit at September 30, 2019. The amounts of undisbursed portions of loans in process at September 30, 2019 were $2.2 million. The Company had a total of $615,000 in standby letters of credit. Also, at September 30, 2019, the Company had no outstanding futures or options positions.

Outstanding letters of credit written are conditional commitments issued by the Company to guarantee the performance of a customer to a third party. The majority of these standby letters of credit expire within the next twelve months. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending other loan commitments. The Company requires collateral supporting these letters of credit as deemed necessary. Management believes that the proceeds obtained through a liquidation of such collateral would be sufficient to cover the maximum potential amount of future payments required under the corresponding guarantees. The current amount of the liability as of September 30, 2019 for guarantees under standby letters of credit issued is not material.

The Company leases land for two of its branch offices. The Company leases office space for three remote offices. Rent expense amounted to $158,000 and $150,000 for the years ended September 30, 2019 and 2018. Minimum rental commitments for the next five years at September 30, 2019, are summarized below:

	Fiscal Year	Rental Amount
		(In thousands)
	2020	**$ 161**
	2021	**163**
	2022	**164**
	2023	**169**
	2024	**179**
Total		**$ 836**

The Company is required to maintain reserve funds in cash or on deposit with the Federal Reserve Bank. The required reserve was $626,000 for the year ended September 30, 2019.

14. LEGAL CONTINGENCIES

Various legal claims also arise from time to time in the normal course of business which, in the opinion of management, will have no material effect on the Company's consolidated financial statements.

15. RESTRICTED RETAINED EARNINGS

At the time of conversion to a stock savings bank, in 1987, the Bank established a liquidation account in an amount equal to the Bank's net worth as reflected in the latest Consolidated Statements of Financial Condition of the Bank contained in the offering circular utilized in the conversion. The function of the liquidation account is to establish a priority on liquidation and, except with respect to the payment of cash dividends on, or the re-purchase of, any of the common stock by the Bank, the existence of the liquidation account will not operate to restrict the use or application of any of the net worth accounts of the Bank. In the event of a complete liquidation of the Bank (and only in such event), each eligible account holder will be entitled to receive a pro rata distribution from the liquidation account, based on such holder's proportionate amount of the total current adjusted balances from deposit accounts then held by all eligible account holders, before any liquidation distribution may be made with respect to stockholders. The liquidation account was approximately $2,300,000 at September 30, 2019. Furthermore, the Company may not repurchase any of its stock if the effect thereof would cause the Company’s net worth to be reduced below (i) the amount required for the liquidation account or (ii) the regulatory capital requirements.

16. FAIR VALUE MEASUREMENTS AND DISCLOSURES

The Company uses fair value measurements to record fair value adjustments to certain assets and liabilities and to determine fair value disclosures. In accordance with accounting guidance, the fair value of a financial instrument is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value is best determined based upon quoted market prices. However, in many instances, there are no quoted market prices for the Company's various financial instruments. In cases where quoted market prices are not available, fair values are based on estimates using present value or other valuation techniques. Those techniques are significantly affected by the assumption used, including the discount rate and estimates of future cash flows. Accordingly, the fair value estimates may not be realized in an immediate settlement of the instrument.

The fair value guidance provides a consistent definition of fair value, which focuses on exit price in an orderly transaction (that is, not a forced liquidation or distressed sale) between market participants at the measurement date under current market conditions. If there has been a significant decrease in the volume and level of activity for the asset or liability, a change in valuation technique or the use of multiple valuation techniques may be appropriate. In such instances, determining the price at which willing market participants would transact at the measurement date under current market conditions depends on the facts and circumstances and requires the use of significant judgment. The fair value is determined at a reasonable point within the range that is most representative of fair value under current market conditions.

The guidance establishes a fair value hierarchy that prioritizes the inputs to valuation methods used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy under are as follows:

Level 1: Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities.

Level 2: Quoted prices in markets that are not active, or inputs that are observable either directly or indirectly, for substantially the full term of the asset or liability.

Level 3: Prices or valuation techniques that require inputs that are both significant to the fair value measurement and unobservable (i.e., supported with little or no market activity).

An asset’s or liability’s level within the fair value hierarchy is based on the lowest level of input that is significant to the fair value measurement.

For financial assets measured at fair value on a recurring basis, the fair value measurements by level within the fair value hierarchy used at September 30, 2019 and 2018 are as follows (in thousands):

Description	**Total**	**(Level 1) Quoted Prices in Active Markets for Identical Assets**	**(Level 2) Significant Other Observable Inputs**	**(Level 3) Significant Unobservable Inputs**
September 30, 2019				
Available for sale securities:				
Collateralized mortgage obligations	**$ 778**	**$ -**	**$778**	**$ -**
U.S. Government money market funds	**2,457**	**2,457**	**-**	**-**
Totals	**$ 3,235**	**$ 2,457**	**$778**	**$ -**

Description	**Total**	**(Level 1) Quoted Prices in Active Markets for Identical Assets**	**(Level 2) Significant Other Observable Inputs**	**(Level 3) Significant Unobservable Inputs**
September 30, 2018				
Available for sale securities:				
Collateralized mortgage obligations	$ 802	$ -	$ 802	$ -
U.S. Government money market funds	74	74	-	-
Totals	$ 876	$ 74	$ 802	$ -

There were no transfers in and out of Level 1 and Level 2 fair value measurements for the year ended September 30, 2019.

For assets measured at fair value on a non recurring basis, the fair value measurements by level within the fair value hierarchy used at September 30, 2019 and 2018 are as follows (in thousands):

Description	September 30, 2019	(Level 1) Quoted Prices in Active Markets for Identical Assets	(Level 2) Significant Other Observable Inputs	(Level 3) Significant Unobservable Inputs
Impaired Loans	$ 9,432	$ -	$ -	$ 9,432
Totals	$ 9,432	$ -	$ -	$ 9,432

Description	September 30, 2018	(Level 1) Quoted Prices in Active Markets for Identical Assets	(Level 2) Significant Other Observable Inputs	(Level 3) Significant Unobservable Inputs
Impaired Loans	$ 10,169	$ -	$ -	$ 10,169
Foreclosed Real Estate	1,043	-	-	1,043
Totals	$ 11,212	$ -	$ -	$ 11,212

Quantitative Information about Level 3 Fair Value Measurements

	September 30, 2019			
Description	**Fair Value**	**Valuation Technique**	**Unobservable Input**	**Range (Weighted Average) (3)**
Impaired loans	**$ 9,432**	**Fair Value of Collateral (1)**	**Appraised Value (2)**	**17% - 27% (18%)**

Quantitative Information about Level 3 Fair Value Measurements

	September 30, 2018			
Description	**Fair Value**	**Valuation Technique**	**Unobservable Input**	**Range (Weighted Average) (3)**
Impaired loans	$ 10,169	Fair Value of Collateral (1)	Appraised Value (2)	17% - 27% (18%)
Foreclosed Real Estate	1,043	Appraised Value (2)	Appraised Value (2)	17%

(1) Fair value is generally determined through independent appraisals of the underlying collateral, which include Level 3 inputs that are not identifiable.
(2) Appraisals may be adjusted by management for qualitative factors such as economic conditions and estimated liquidation expenses.

The significant unobservable inputs for impaired loans are the appraised value or an agreed upon sales price. These values are adjusted for estimated costs to sell which are incremental direct costs to transact a sale such as broker commission, legal fees, closing costs and title transfer fees. The costs must be considered essential to the sale and would not have been incurred if the decision to sell had not been made. The costs to sell are based on costs associated with the Company’s actual sales of other real estate owned which are assessed annually.

Other real estate owned is measured at fair value, less costs to sell at the date of foreclosure, establishing a new cost basis. Subsequent to foreclosure, valuations are periodically performed by management and the assets are carried at the lower of the carrying amount or fair value, less costs to sell.

The following information should not be interpreted as an estimate of the fair value of the entire Company since a fair value calculation is only provided for a limited portion of the Company’s assets and liabilities. Due to a wide range of valuation techniques and the degree of subjectivity used in making the estimates, comparisons between the Company’s disclosures and those of other companies may not be meaningful. The following methods and assumptions were used to estimate the fair values of the Company’s financial instruments at September 30, 2019 and 2018.

Cash and Cash Equivalents (Carried at Cost)

The carrying amounts reported in the Consolidated Statements of Financial Condition for cash and short-term instruments approximate those assets' fair values.

Securities

The fair value of securities available for sale (carried at fair value) and held to maturity (carried at amortized cost) are determined by obtaining quoted market prices on nationally recognized securities exchanges (Level 1), or matrix pricing (Level 2), which is a mathematical technique used widely in the industry to value debt securities without relying exclusively on quoted prices for the specific securities but rather by relying on the securities' relationship to other benchmark quoted prices. The Company currently holds U.S. Government money market funds which are classified as Level 1, because quoted prices are available for these securities in an active market.

The Bank’s investment portfolio is maintained by a third-party which utilizes Interactive Data Corporation (IDC) as its primary source for security valuations. IDC is not affiliated with or owned by a securities broker, dealer or underwriter, nor is it actively involved in the business of investment management or securities trading. Some of the major asset classes that IDC provides pricing and market inputs are as follows: U.S. Agency/Government Sponsored Enterprise (GSE) issues, U.S. high grade municipal issues, and U.S. Structured Securities Agency/GSE Collateralized Mortgage Obligation issues. The methodology used to price the above asset classes include: broker quotes, proprietary modes, vast descriptive terms and conditions databases, as well as extensive quality control programs. Market inputs used to help determine the fair value hierarchy include but not limited to: security characteristics, ratings updates, prepayment schedules; cash flows and yield to maturity. Based on these methodologies employed by IDC; the Company considers these evaluations Level 2 in reference to ASC 820 with the exception of inactive markets. There are no securities in an inactive environment.

Loans Receivable (Carried at Cost)

The fair values of loans, excluding impaired loans are estimated using discounted cash flow analyses, using market rates at the Consolidated Statements of Financial Condition date that reflect the credit and interest rate-risk inherent in the loans. Projected future cash flows are calculated based upon contractual maturity or call dates, projected repayments and prepayments of principal. Generally, for variable rate loans that reprice frequently and with no significant change in credit risk, fair values are based on carrying values.

Impaired loans are those loans which the Company has measured impairment generally based on the fair value of the loan’s collateral. Fair value is generally determined based upon independent third-party appraisals of the properties, or discounted cash flows based upon the expected proceeds. These assets are included as Level 3 values, based upon the lowest level of input that is significant to the fair value measurements.

Federal Home Loan Bank Stock (Carried at Cost)

The carrying amount of this restricted investment in bank stock approximates fair value, and considers the limited marketability of this security.

Bank Owned Life Insurance

Fair value is equal to the cash surrender value of the life insurance policies.

Accrued Interest Receivable and Payable (Carried at Cost)

The carrying amount of accrued interest receivable and accrued interest payable approximates their fair value.

Deposit Liabilities (Carried at Cost)

The fair values disclosed for demand deposits (e.g., interest and noninterest checking, passbook savings and money market accounts) are, by definition, equal to the amount payable on demand at the reporting date (i.e., their carrying amounts). Fair values for fixed-rate certificates of deposit are estimated using a discounted cash flow calculation that applies interest rates currently being offered in the market on certificates to a schedule of an aggregated expected monthly maturities on time deposits.

Borrowings (Carried at Cost)

The fair value of short-term borrowings approximates the current book value. Fair values of long-term borrowings are estimated using discounted cash flow analysis, based on quoted prices for new advances with similar credit risk characteristics, terms and remaining maturity. These prices obtained from this active market represent a market value that is deemed to represent the transfer price if the liability were assumed by a third party.

Off-Balance Sheet financial Instruments (Disclosed at Cost)

Fair values for the Company's off-balance sheet financial instruments (lending commitments and letters of credit) are based on fees currently charged in the market to enter into similar agreements, taking into account, the remain terms of the agreements and the counterparties' credit standing. The fair value of these off-balance sheet financial instruments are not considered material as of September 30, 2019 and 2018.

The fair value amounts have been determined by the Company using available market information appropriate valuation methodologies. However, considerable judgment is necessarily required to interpret the data to develop the estimates.

The carrying amounts and fair values of all the Company's financial instruments that are not required to be measured or reported at fair value on the Company's Consolidated Statements of Financial Condition as of September 30, 2019 and 2018 are as follows:

			Fair Value Measurements at September 30, 2019		
(In thousands)	Carrying Amount	Estimated Fair Value	Quoted Prices in Active Markets For Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:					
Cash and cash equivalents	**$ 21,287**	**$ 21,287**	**$ 21,287**	**$ -**	**$ -**
Securities held to maturity	**114,415**	**115,447**	**-**	**115,447**	**-**
Loans receivable - net	**604,784**	**614,502**	**-**	**-**	**614,502**
Federal Home Loan Bank stock	**5,058**	**5,058**	**5,058**	**-**	**-**
Bank-owned life insurance	**16,862**	**16,862**	**16,862**	**-**	**-**
Accrued interest receivable	**2,079**	**2,079**	**2,079**	**-**	**-**
Liabilities:					
Checking, passbook, club and NOW deposit accounts	**183,908**	**183,908**	**183,908**	**-**	**-**
Money Market deposit accounts	**205,779**	**205,779**	**205,779**	**-**	**-**
Certificate of deposit accounts	**196,655**	**196,951**	**-**	**-**	**196,951**
Short-term borrowings	**8,830**	**8,830**	**8,830**	**-**	**-**
Long-term borrowings	**102,295**	**103,906**	**-**	**-**	**103,906**
Accrued interest payable	**223**	**223**	**223**	**-**	**-**
Off-balance sheet financial instruments	-	-	**-**	**-**	**-**

			Fair Value Measurements at September 30, 2018		
(In thousands)	Carrying Amount	Estimated Fair Value	Quoted Prices in Active Markets For Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:					
Cash and cash equivalents	$ 8,076	$ 8,076	$ 8,076	$ -	$ -
Securities held to maturity	107,042	103,946	-	103,946	-
Loans receivable - net	615,899	611,279	-	-	611,279
Federal Home Loan Bank stock	5,286	5,286	5,286	-	-
Bank-owned life insurance	16,464	16,464	16,464	-	-
Accrued interest receivable	2,239	2,239	2,239	-	-
Liabilities:					
Checking, passbook, club and NOW deposit accounts	175,413	175,413	175,413	-	-
Money Market deposit accounts	217,177	217,177	217,177	-	-
Certificate of deposit accounts	189,488	185,809	-	-	185,809
Short-term borrowings	17,207	17,207	17,207	-	-
Long-term borrowings	91,309	88,578	-	-	88,578
Accrued interest payable	179	179	179	-	-
Off-balance sheet financial instruments	-	-	-	-	-

17. PARENT COMPANY ONLY CONDENSED FINANCIAL INFORMATION

Condensed financial statements of Harleysville Financial Corporation are as follows:

(In thousands)	September 30,	
Condensed Statements of Financial Condition	**2019**	**2018**
Assets		
Cash	**$ 67**	$ 5
Investment in subsidiary	**76,262**	71,914
Total Assets	**$ 76,329**	$ 71,919
Liabilities and Stockholders' Equity		
Other liabilities	**$ 82**	$ 81
Stockholders' equity	**76,247**	71,838
Total Liabilities and Stockholders' Equity	**$ 76,329**	$ 71,919

	For the Year Ended September 30,	
Condensed Statements of Income:	**2019**	**2018**
Equity in income of subsidiary	**$ 4,352**	$ 3,054
Distributed earnings of subsidiary	**4,540**	4,750
Other expense	**743**	694
Net income	**$ 8,149**	$ 7,110

	For the Year Ended September 30,	
Condensed Statements of Cash Flows	**2019**	**2018**
Net income	**$ 8,149**	$ 7,110
Increase in other liabilities	**1**	4
Stock based compensation	**309**	258
Equity in undistributed earnings of subsidiary	**(4,352)**	(3,054)
Net cash provided by operating activities	**4,107**	4,318
Financing activities:		
Acquisition of treasury stock	**(651)**	(1,461)
Sale of treasury stock delivered under employee stock plans	**294**	461
Dividends paid	**(3,688)**	(3,426)
Net cash used in financing activities	**(4,045)**	(4,426)
Increase(decrease) in cash and cash equivalents	**62**	(108)
Cash and cash equivalents at the beginning of the period	**5**	113
Cash and cash equivalents at the end of the period	**$ 67**	$ 5

18. Revenue Recognition

On October 1, 2018, the Company adopted ASU No. 2014-09 "Revenue from Contracts with Customers" (Topic 606) and all subsequent ASUs that modified Topic 606. As stated in Note 2 Summary of Significant Accounting Policies, the implementation of the new standard did not have a material impact on the measurement or recognition of revenue; as such, a cumulative effect adjustment to opening retained earnings was not deemed necessary. Results for reporting periods beginning after October 1, 2018 are presented under Topic 606, while prior period amounts were not adjusted and continue to be reported in accordance with our historic accounting under Topic 605.

Topic 606 does not apply to revenue associated with financial instruments, including revenue from loans and securities. In addition, certain noninterest income streams such as income from bank owned life insurance, sales of investment securities, and certain items within other income are also not in scope of the new guidance. Topic 606 is applicable to noninterest revenue streams such as deposit related fees and interchange fees. However, the recognition of these revenue streams did not change significantly upon adoption of Topic 606.

The following table presents noninterest income for the year ended September 30, 2019 and 2018:

(Dollars in thousands)	Year Ended September 30,	
Non-Interest Income	**2019**	**2018**
In-scope of Topic 606:		
Fee income	**$ 138**	$ 130
Insufficient fund fees	**485**	474
Interchange fee income	**826**	744
Gain on sale of foreclosed real estate	**467**	304
Other income	**294**	342
Total Non-Interest Income (in-scope of Topic 606)	**2,210**	1,994
Out-of-scope of Topic 606:		
Increase in cash surrender value of bank-owned life insurance	**398**	393
Gains on sales of securities	**144**	-
Other	**331**	479
Total Non-Interest Income (out-scope of Topic 606)	**873**	872
Total Non-Interest Income (in-scope of Topic 606)	**2,210**	1,994
Total Non-Interest Income	**$ 3,083**	$ 2,866

The following is a discussion of key revenues of fees for customer services that are within the scope of the new revenue guidance:

- *Fee income* – Fees include service charges on deposits and consist of transaction-based fees, debit card replacement fees, Automated Clearing House (ACH) fees and account maintenance fees for various retail and business checking customers. These fees are charged as earned on the day of the transaction or within the month of the service.

- *Insufficient funds fees and other income*– Revenue from service charges on deposit accounts is earned through cash management, wire transfer, ATM fees and other deposit-related services; as well as overdraft, non-sufficient funds and account management fees. Revenue is recognized for these services either over time, corresponding with deposit accounts' monthly cycle, or at a point in time for transactional related services and fees. These revenues are included in insufficient funds fees and other income in the table above.

- I*nterchange fee income* – Fees generated when Company cardholders conduct transactions on their debit cards with merchants for goods or services. The Company then collects a portion of the fees generated from those transactions. Revenue is recognized for these transactions within the month they transpire.

- *Gain on sale of foreclosed real estate* – Revenue from the sale of a foreclosed property is recognized at the time the property is sold or within the month the transaction occurs. The Company does not finance the sale of the loan to obtain the property.

19. SUBSEQUENT EVENTS

Management has reviewed events occurring through December 3, 2019, the date the financial statements were issued, and no subsequent events occurred requiring accrual or disclosures.